CANADIAN TRADE NEGOTIATIONS

INTRODUCTION

SELECTED DOCUMENTS

FURTHER READING

MINISTER
FOR
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SECRETARY OF STATE
FOR
EXTERNAL AFFAIRS

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DEPARTMENT OF EXTERNAL AFFAIRS
DECEMBER 15, 1985

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CANADIAN TRADE NEGOTIATIONS

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OTTAWA
December 15, 1985

FOREWORD

The government decided in September that Canada should proceed to serious examination with the United States government of the potential scope and prospects for a comprehensive trade agreement with the United States, concurrent with ongoing efforts to launch a new round of multilateral trade negotiations.

The Quebec Trade Declaration charged the Minister for International Trade to "chart all possible ways to reduce and eliminate existing barriers to trade" between Canada and the United States. Since March, we have pursued this mandate by consulting widely, examining a broad range of policy issues, and meeting informally with our U.S. counterparts and other trading partners.

Public consultations across the country, and discussions with business organizations and the provinces, demonstrated a widespread dissatisfaction with the status quo. Uncertainty about access to the United States market was considered a key element in Canadian economic performance. In addition, many Canadians referred to the need to gain access to a larger market so that Canadian industry can benefit from economies of scale and increase its ability to compete in the wider world market. These views are strongly held despite the fact that Canada over the last three years has run a large merchandise trade surplus with the United States. The merchandise trade surplus, of course, is to a large degree balanced by the deficit in trade in services and capital flows. Traditionally, Canada has run an overall current account deficit with the United States. Our recent success in the U.S. market has now made more Canadian firms aware of our vulnerability to U.S. protectionism. At the same time, there are an increasing number of firms who are confident of their ability to compete in the larger North American market and in overseas markets but who feel threatened by the U.S. protectionist surge.

The following pages present in one place a number of basic documents that help to explain the government's decision to pursue negotiations with the United States with a view to further expanding trade to the mutual advantage of both countries. In addition to those documents which have already been made publicly available in one form or another, such as the recommendations of the Special Joint Parliamentary Committee on Canada's International Relations, the conclusions and recommendations of the Royal Commission on the Economic Union and Development Prospects for Canada (the Macdonald Commission), the reports of International Trade Minister Kelleher and United States Trade Representative Clayton Yeutter, this collection includes reports on the extensive Canada-wide consultations undertaken by the Minister for International Trade and by the Special Coordinator for Market Access Consultations, Mr. Tom Burns. In addition, it includes an internal government document used as the basic point of departure for much of the analytical work pursued over the course of the summer, a statement by the Secretary of State for External Affairs on trade negotiations as they may involve cultural industries and to aid readers not familiar with Canadian trade policy, a glossary of technical terms and some suggestions for further reading.

This booklet is being made available in order to facilitate informed debate on one of the most important issues of public policy facing the country. As noted by the Prime Minister in his letter of October 1, 1985 to President Reagan, " the negotiation of a new trade agreement will, of course, be extremely arduous. The challenge to succeed, however, and the fruits of success, are well worth the enormous effort and good faith required for this initiative." For this initiative to succeed in its fundamental purpose of substantially advancing the interests of the Canadian people, it obviously must command a strong measure of public support. It is our hope that this document will help to provide a basis of understanding that will contribute to the mobilization of that support. Over the coming months and years, therefore, the government would welcome comment and advice from interested Canadians.

J Kelleher

Minister for
International Trade

Secretary of State for
External Affairs

PART I:

INTRODUCTION

Canadians face an historic choice. Governments can carry on with a policy of bailing out failing firms in declining industries and choose to do nothing to gain more secure access to the U.S. market; but only at the expense of jeopardizing many thousands of the two million jobs now directly dependent on export sales south of the border.

The better and safer bet would be to try to negotiate a freer trade agreement with the U.S. that would open up new opportunities for productive Canadian firms and businesses, while also safeguarding social, cultural and political values essential to our Canadian identity.

London Free Press, September 28, 1985

CANADA-UNITED STATES TRADE NEGOTIATIONS: THE ISSUES AND THE PROCESS

The United States market, some 15 times larger than that of Canada in terms of consumption, is one of the largest factors affecting the health of the economy, accounting for a quarter of GNP and upwards of two million jobs. Access to that market is not considered to be sufficiently secure and, on occasion, threatens to become less so. There are indications that the situation will not improve unless the government takes a concerted approach to reduce or eliminate existing and threatened barriers.

Last year protectionist threats and measures (quotas, anti-dumping and countervailing duties, surcharges) affecting Canada included steel and steel pipes, copper and sugar products in Ontario, asbestos in Quebec, raspberries in British Columbia, rock salt and salt cod in the Maritimes, and softwood lumber and hogs in virtually all regions of Canada. Almost $6 billion of Canadian exports to the U.S. or 6% of the total were involved. The industries concerned provided some 146,000 jobs, a significant proportion of which were at risk.

The principal concern fuelling interest in a trade negotiation, therefore, is that Canadian jobs are lost when the United States imposes quotas or higher tariffs on trade. Canada requires an agreement that exempts our exports from U.S. protectionist measures aimed at reducing the imports of other countries. Such an agreement should also reduce the severity and duration of any measures aimed specifically at Canada and should limit the ability of the United States unilaterally to determine the terms of cross-border trade. Proposals before Congress to impede Canadian exports of lumber to the United States valued at $3 billion a year, afford a good example of the reality of the U.S. threat in 1985.

If the U.S. were to impose across-the-board trade restrictions as a means of reducing its trade deficit of some $130 to $150 billion, the effect on Canadian employment could be dramatic. It is estimated that a 10% reduction of our exports alone could cause up to 250,000 Canadians to lose their jobs.

This new protectionist threat comes on top of an existing system of so-called contingency protection measures that pose an ever-present threat to many Canadian exports. Many Canadian companies doing business in the United States find themselves compelled to hire expensive Washington law firms as their U.S. competitors increasingly use the full array of U.S. trade remedy law in an effort to obtain relief from foreign competition.

A further reason for pursuing negotiations, of significance whether the mood in Washington is protectionist or not, is to increase Canadian access to the huge

U.S. market in order to stimulate either new or renewed investment in this country, increase the efficiency and competitiveness of Canadian companies and thus expand both employment and incomes in Canada. New jobs are created and new investment is stimulated when the market is large enough to allow economies of scale and specialized production. Better jobs are created when companies are confident about the future and are prepared to restructure to remain competitive. The vast majority of Canadian firms are confident they can meet the challenge of competing in a larger market.

The elimination of existing U.S. tariffs, import quotas and other barriers such as Buy America restrictions would give Canadian industry unimpeded and more secure access to a market of some 250 million people. It would make Canada a more attractive place to invest, not only by Canadians but by Americans, Europeans, Japanese and others who regard more secure access to a large market as a prerequisite to profitable, employment-creating enterprises. A recent survey of Canadian companies with investments in the United States showed that the threat of tariffs, quotas and other restrictions in the United States will be a key factor in future decisions about whether to invest either in Canada or the United States.

High U.S. tariffs -- 15% and more on petrochemicals, rolling stock, clothing and many other products -- continue to raise barriers to the U.S. market that prevent Canadian firms from achieving the economies of scale on which increased competitiveness and employment in Canadian industry so vitally depends. It has been frequently noted that once the Tokyo Round tariff reductions have been fully implemented in 1987, some 80% of Canada's exports to the U.S. will enter duty-free and a further 15% at duties of 5% or less. This calculation, based on 1976 trade patterns, masks the fact that certain products are not traded because of high tariffs but could be if the barriers were lowered. Nevertheless, the changing composition of Canadian exports has already lowered the estimate to 70% duty-free. The major changes in the exchange rate since 1976 have made it possible for many Canadian firms to jump over 5% and even 10% tariffs and compete in sectors from which they were previously excluded. Removal of remaining tariff barriers would further assist competitive Canadian companies to penetrate the U.S. market. Finally, the existence of Canadian tariffs on imports from the United States is often costly to Canadian customers because Canadian producers typically charge their Canadian customers the U.S. price plus the Canadian tariff.

A further inhibiting factor is the lack of an adequate dispute settlement mechanism. While the General Agreement on Tariffs and Trade (GATT) provides a basis for resolving disputes, it does so only after most of the damage has been done and following a long and cumbersome process. It can do little to control congressionally inspired protectionism. Current differences of view regarding, for example, resource management, such as stumpage practices for the forest industry, are being dealt with on an ad hoc basis and at substantial legal and lobbying cost to the industry. Even individual states have taken actions adversely affecting Canadian export interests. What is needed is a system that deals more fairly, expeditiously and conclusively with these kinds of disputes on both sides of the border.

WHAT CANADA WILL BE SEEKING

The primary objective in any trade negotiation with the United States, therefore, would be to protect existing Canadian jobs and stimulate the creation of new jobs. These twin objectives arise from the two concerns outlined above: the current and recurrent threat of U.S. protectionism which could reduce access to the U.S. market on which a quarter of Canada's prosperity depends and the need to stimulate restructuring of the Canadian economy to keep pace with international competitive pressures. The ultimate effect should be a more positive and predictable foundation of rules and procedures for our predominant trade relationship by committing Congress and the Administration to a jointly negotiated agreement. To this end, in a trade negotiation, Canada will seek:

To secure our market access through:

- new rules and procedures limiting the protectionist effect of trade remedy laws, i.e., exemption from measures aimed at others and a rigorous limitation on the degree and duration of measures which affect Canada; and

- clearer definition of countervailable financial assistance programs (i.e., subsidies) to industry, agriculture and fisheries so as to reduce the threat of countervailing duties.

To enhance our market access through:

- more open entry to the U.S. federal and state government procurement markets; and

- broad trade liberalization, in an orderly manner, through the elimination of tariffs and quotas to be achieved over a reasonable period of time with adequate adjustment transition provisions. Current barriers inhibit full Canadian industry participation in the North American market and in this way prevent Canadian companies from achieving the efficient large-scale production that could enable them to compete more effectively in U.S. markets and other markets around the world.

To enshrine our market access through:

- a strong dispute settlement mechanism to reduce the disparities in size and power and to provide fair, expeditious and conclusive solutions to differences of view and practice;
- institutional and other provisions that maintain Canadian independence of action in areas of national endeavour; and
- a treaty or congressional-executive agreement to enshrine our mutual obligations and accomodate differences in the two governmental systems.

> **This Canadian initiative would not be an act of desperation but of confidence. A Canada-United States Free Trade Agreement offers the most promising opportunity to create a more efficient, adaptive, and outward-looking Canadian -- and U.S. -- economy that would provide rising living standards and expanding employment opportunities for the great majority of people. Its success would demonstrate to the rest of the world that trade liberalization, rather than rising protectionism, remains -- as it has since World War II -- the practical key to prosperity.**
>
> **Richard Lipsey and Murray Smith, Taking the Initiative: Canada's Trade Options in a Turbulent World.**

HOW WE INTEND TO PROCEED

The broad interests and objectives of the United States Administration regarding bilateral trade between Canada and the United States are spelled out in the report of U.S. Trade Representative Yeutter to the President and in the President's reply to the Prime Minister in the fall of 1985. These interests and objectives flow from issues that arise in the management of the largest bilateral trading relationship in the world. They are similar to issues that the Administration is also pursuing multilaterally.

The quid pro quo that the United States is likely to seek in return for securing and enhancing Canadian access to its market is freer and more secure access to the Canadian market. The U.S. Administration has indicated it is prepared to consider our key concerns (such as the effect on Canada of U.S. trade remedy laws such as anti-dumping and countervailing duties and other safeguards, elimination of Buy America restrictions, a strong dispute settlement mechanism and strong institutions to safeguard our sovereignty), as long as we are prepared to consider their key objectives (such as mutual elimination of tariffs, and new disciplines on investment and services). The role and extent of subsidy practices would also be a central negotiating issue in efforts to limit the application of U.S. trade remedy laws to Canada. There is also a list of issues where there is room for improvement but which would be largely neutral. These would include intellectual property rights, standards, and regulatory requirements.

Whether or not the Administration will be able to meet our objectives and Congress will be prepared to pass enacting legislation cannot now be judged. At a minimum, it will require extensive exploratory negotiations.

More secure and enhanced access to each other's markets and commitments regarding investment and services are the areas in which the scope for defining an acceptable agreement will be determined through formal negotiations.

The Prime Minister announced the government's interest in pursuing a new trade agreement with the United States in the House of Commons on Thursday, September 26, 1985. Mr. Kelleher's report to the Prime Minister and United States Trade Representative Yeutter's report to the President called for by the Declaration on Trade issued by the two leaders in Quebec City on March 18, 1985 have been publically released.

On October 1, 1985 the Prime Minister wrote to the President to propose formally that Canada and the United States pursue an agreement involving the broadest possible package of mutually beneficial reductions in barriers to trade in goods and services. On October 2, the President replied, welcoming this proposal and indicating that the Administration was now proceeding with consultations with the Congress and the private sector as to their views regarding negotiations with Canada.

THE UNITED STATES PROCESS

Under the U.S. constitution, Congress has exclusive authority to regulate interstate and international commerce. It is an authority which it guards with care. At the same time, modern trade negotiations require the executive branch to be able to conduct negotiations for the United States. Since 1934, therefore, with passage of the *Reciprocal Trade Agreements Act*, the Congress has periodically delegated its authority to the Administration. It does this, however, only for specified periods of time and within clearly defined limits.

The U.S. Administration's current authority derives from the most recent series of trade acts: the *1974 Trade Act*, which provided the basic authority for participation in the Tokyo Round; the *1979 Trade Agreements Act*, which passed into U.S. law the results of the Tokyo Round; and the *1984 Trade and Tariffs Act*, which amended certain provisions of the previous two Acts, including those related to the Administration's negotiating authority.

The general negotiating authority in the 1974 *Trade Act* was extended and enlarged by the *1984 Trade and Tariffs Act* to 1988. The general authority allows the President to negotiate such agreements as are in the U.S. interest which include non-tariff barriers. In order to help the President identify U.S. interests, Congress has laid out a series of objectives to which an agreement must respond. These include:

- more open and equitable market access and the harmonization, reduction or elimination of trade distorting measures in the agricultural and industrial sectors;
- competitive opportunities for U.S. exports in developed countries equivalent to the opportunities afforded their imports in U.S. markets;
- bilateral trade agreements providing for mutually advantageous economic benefits;
- international rules and procedures on the use of temporary safeguard measures;
- trade agreements to assure U.S. access at reasonable prices to necessary supplies;
- trade agreements to reduce or eliminate barriers or other distortions to, and to develop internationally agreed rules on, trade in services and foreign direct investment;
- trade agreements with respect to high-technology products, to eliminate or reduce foreign barriers to exports or investment; and
- trade agreements to achieve various commitments, such as on foreign procurement, national treatment, and joint scientific cooperation, and

effective minimum safeguards for acquisition and enforcement of intellectual property rights.

Special provisions known as the fast-track procedures allow the President to negotiate trade agreements, notify the Congress 90 days in advance that he intends to enter into an agreement and publish his intent in the Federal Register. After entering into the Agreement, he must report he has done so to the Congress and forward any necessary enabling legislation to the Congress. Congress then has a further 60 days to approve or reject the agreement and to enact the enabling legislation.

If a bilateral agreement to be processed under the fast-track procedures is to provide for more than incidental duty reductions, the initiative must come from the other country. The President must then notify the Congress 60 days before the start of the 90-day period that he intends to negotiate duty reductions at the other country's request. He may proceed at the end of 60 days unless he has been advised to the contrary by the Congress. The length of time available between the end of the initial 60-day period and 90-day period is not specified. The President on December 10, 1985 wrote to the Chairmen of the House Ways and Means Committee and the Senate Finance Committee of his intention to enter into trade negotiations with Canada.

An agreement that includes duty reductions requires greater congressional liaison throughout, as well as a report from the International Trade Commission (ITC) on the likely impact of such an agreement on U.S. industry. The ITC conducted such an investigation pursuant to the 1984 Canadian request for sectoral negotiations. Such an agreement also requires advice from the private sector advisory structure.

> **A national vote in favour of bilateral free trade would represent the ultimate declaration by Canadians of self-confidence in themselves, confidence both in their ability to compete and in their ability to continue as a distinct political and social unit.**
>
> **Richard Gwyn, The 49th Paradox**

PREPARING FOR NEW MULTILATERAL TRADE NEGOTIATIONS

Concurrent with efforts to prepare for and pursue negotiations with the United States, the Government of Canada will continue its efforts, in cooperation with a large number of other countries, including the United States, to launch a new round of multilateral trade negotiations under the auspices of the General Agreement on Tariffs and Trade. These negotiations will have many of the same objectives as those with the United States, but worked out on a broader scale and involving many more countries. While the broad objectives will be the same, the means and focus will be different. The challenge for Canada will be to ensure a coordinated and integrated approach so that we will get the best overall deal out of both negotiations.

NEXT STEPS

The next steps fall under two headings. First, the establishment of a negotiating team under the overall direction of the recently appointed Chairman of the Preparatory Committee, Mr. Simon Reisman. Mr. Reisman will report to a special Cabinet Committee under the chairmanship of the Secretary of State for External Affairs. His first tasks will be to build a negotiating team, consult closely with the provinces, particularly in respect of those matters falling under provincial jurisdiction that are expected to come up in negotiations, and build on the earlier consultations with business, labour and other groups through the new International Trade Advisory Committee and the Sectoral Advisory Groups, described below.

The second step involves the undertaking by Mr. Reisman of detailed preparatory work, on the basis of existing analysis and reports, and subsequently carrying out the negotiations with the United States if there is joint agreement by the two countries that they should proceed. That preparatory work will serve both the proposed Canada-United States negotiations and the new round of negotiations to be undertaken under GATT. Current projections suggest that a new round of multilateral negotiations may be formally launched before the end of 1986. Discussions with the United States may commence in the early part of that year.

INTERNATIONAL TRADE ADVISORY COMMITTEE (ITAC) SYSTEM

Concurrent with the government's decision to explore more directly with the United States the scope and prospects for a new trade agreement, the government announced it is establishing an International Trade Advisory

Committee System. The purpose in establishing this advisory committee system is to provide a two-way flow of information and advice between the government and the private sector on international trade matters. The advisory committees will address international trade access and marketing issues on both a bilateral and multilateral basis. In setting up this system, the Minister for International Trade is responding to the wishes of business, labour, consumers and others to have a permanent, ongoing mechanism for regular consultation with the federal government on international trade matters.

This committee system will have an important advisory role to play in the ongoing discussions. Similarly, it will also be asked to advise on multilateral trade negotiations under GATT. This committee system should reassure the private sector that their concerns, including specific sectoral interests, are being effectively addressed and that the federal government has the benefit of their advice on the implications of change.

The advisory structure will comprise two components. There will be a 25-30 member group, the International Trade Advisory Committee (ITAC), that will concern itself with broad national issues relating to international trade access and marketing matters. Walter Light, former Chairman of Northern Telecom Ltd., has been appointed Chairman of ITAC by the Minister for International Trade. The other component will consist of a series of Sectoral Advisory Groups on International Trade (SAGITs), which will interact with the government to ensure that sectoral views are fully taken into account on international trade matters.

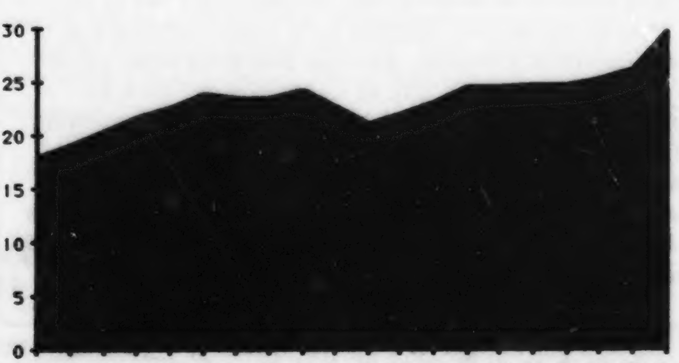
> **"It is often alleged that those supporting liberalized trade 'have not done their homework.' In reality, that is far more true of those who oppose free trade. Among the critics, therefore, rhetoric, passion and a maudlin nationalism sometimes fill the gap or conceal a defence of economic privilege. That does not pay the issue anything like its due.**
>
> **Who are the real "nationalists" in the free trade debate, and who are the defenders of special interests? Who has done the research, and who appeals to generalized fears? A debate exists; its quality is the problem."**
>
> **Globe and Mail, November 18,1985**

CONCLUSIONS

The government has decided it will embark on this course because it is convinced that a process of bilateral and multilateral negotiations, proceeding in tandem, will best achieve Canada's need to secure and enhance its access to export markets. By this means, Canadian manufacturing industry, forestry, agriculture and fisheries will have the marketing environment by which they can restructure, expand and prosper in a stable trading world and in so doing, save jobs now, and create new jobs in the future. These initiatives will, moreover, serve to dampen protectionist initiatives, especially in the United States, which threaten or could damage important Canadian interests. Negotiations concentrating on bilateral trade and trade policy issues would focus attention in the United States on Canadian economic and trade problems, and on the important U.S. stake in the Canadian economy. Also, by embarking on negotiating now, the two countries would also reinforce broader international efforts to open a new round of tariff and trade negotiations within GATT. Throughout the negotiations, the government will be ruled by one fundamental objective: the benefits must be mutual and they must be substantially greater than the costs. To be acceptable, the final package will have to serve the best interests of the Canadian people and every region of the country.

CHART 1

CANADIAN EXPORTS AS PERCENT OF GNP: 1965-1984



PART II:

SELECTED DOCUMENTS

> Amid all this, the prime minister of Canada, Brian Mulroney, came forward with a proposal that, unlike all these other tangles, Reagan might be able to do something about.
>
> Okay, says the new Canadian prime minister. Let's stop fussing about our differences in the press, Congress and the Parliament. Let's get some knowledgeable guys together and show the world what freedom and cooperation can really accomplish.
>
> James Reston, New York Times, October 1,

March 18, 1985 **Quebec City**

DECLARATION BY THE PRIME MINISTER OF CANADA AND THE PRESIDENT OF THE UNITED STATES OF AMERICA REGARDING TRADE IN GOODS AND SERVICES

We embark today on a joint effort to establish a climate of greater predictability and confidence for Canadians and Americans alike to plan, invest, grow and compete more effectively with one another and in the global market.

We are convinced that an improved and more secure climate for bilateral trade relations will encourage market forces to achieve a more rational and competitive production and distribution of goods and services.

We remain committed to the principles of the multilateral trading system embodied in the General Agreement on Tariffs and Trade as the cornerstone of our respective trade policies. We are determined to exercise the political will to make the open, multilateral trading system work better and to strengthen and extend the disciplines governing international commerce.

We will work jointly to strengthen the effectiveness of GATT rules and establish new disciplines. We call on all nations to join with us in establishing a preparatory committee this summer for a new round of multilateral trade negotiations to ensure that negotiations commence in early 1986.

We believe that the challenge to our two countries is to invigorate our unique economic relationship. We intend to build on our success in resolving a number of disputes and achieve something of lasting significance to provide a model to other nations of the way in which two modern societies can work in harmony.

We have today agreed to give the highest priority to finding mutually acceptable means to reduce and eliminate existing barriers to trade in order to secure and facilitate trade and investment flows.

As a first step, we commit ourselves to halt protectionism in cross-border trade in goods and services.

We have charged Ambassador Brock, the United States Trade Representative, and the Honourable James Kelleher, Minister for International Trade, to establish immediately a bilateral mechanism to chart all possible ways to reduce and eliminate existing barriers to trade and to report to us within six months.

We have also directed that action be undertaken over the next twelve months to resolve specific impediments to trade in a manner consistent with our international obligations and our legislative requirements. Such action will proceed on the basis of full consultation with the private sector and other levels of government and will concentrate initially on:

- National Treatment, on a contractual, equitable and mutually advantageous basis, with respect to government procurement and funding programs;
- Standardization, reduction or simplification of regulatory requirements which would facilitate trade in goods and services;
- Improvement in the Canada-United States Air Transport Agreement aimed at facilitating transborder travel and commerce by expanding the number of available services and reducing obstacles to the introduction of innovative and competitive new services;
- Strengthening our market approach to Canada-United States energy trade by reducing restrictions, particularly those on petroleum imports and exports, and by maintaining and extending open access to each other's energy markets, including oil, natural gas, electricity and coal;
- Improving access for traders on both sides of the border through reduction in tariff barriers;
- Facilitation of travel for business and commercial purposes;
- Elimination or reduction of tariff and non-tariff barriers to trade in high-technology goods and related services, such as computers, data flow and computer-assisted design and manufacturing technology; and
- Cooperation to protect intellectual property rights including trade in counterfeit goods and other abuses of copyright and patent law.

We urge our respective private sectors to expand their contacts and continue to provide advice on the future of our trading relationship.

We are confident that these undertakings will facilitate trade and investment flows between our two countries and act as catalysts for broader international cooperation.

REPORT ON PUBLIC CONSULTATIONS BY THE MINISTER FOR INTERNATIONAL TRADE*

The Discussion Paper, *How to Secure and Enhance Canadian Access to Markets*, served as a catalyst to a consultative process that took the Minister for International Trade to fifteen cities across Canada, including Vancouver, Calgary, Edmonton, Saskatoon, Winnipeg, London, Kitchener, Toronto, Sudbury, Montreal, Quebec City, Moncton, Halifax, Charlottetown, and St. John's. Undertaken during the period between March 18 and May 3, 1985 the consultations normally involved a confidential meeting with private sector representatives, an open public meeting and a speech to a business group. The Minister for International Trade saw all his provincial counterparts in their respective provinces save his Saskatchewan colleague. Private meetings were held with regional labour leaders in Vancouver, Toronto and Montreal. Whereas the consultations addressed both market access and export financing questions, this report addresses market access only.

During the month of May, the Minister for International Trade met privately with sixteen national trade associations including the Canadian Chamber of Commerce, the Canadian Pulp and Paper Association, the Fisheries Council of Canada, the Canadian Federation of Agriculture, the Grocery Products Manufacturers of Canada, five cultural associations (Canadian Independent Record Production Association, Association du disque et de l'industrie du spectacle québécois, Canadian Film and TV Association, Association of Canadian Publishers, and Canadian Periodical Publishers), the Canadian Petrochemical Producers Association, the Canadian Manufacturers Association, the Canadian Export Association, the Canadian Association of Consumers, the Canadian Labour Congress, and the Business Council on National Issues. The Canadian Federation of Independent Business was undertaking a membership survey on market access questions and did not wish to participate in consultations until this was complete, i.e., in early summer.

Numerous letters were addressed to the Minister for International Trade on the Discussion Paper. Less than 40% contained sufficient detail or commentary to be considered briefs. Approximately half the letters came from Ontario; Quebec and Alberta each accounted for 10%; and British Columbia 7%. About 20% of the submissions came from national associations.

Throughout the consultative process all regions encouraged active Canadian participation in the emerging Multilateral Trade Negotiations (MTN). With specific reference to Canada-U.S.trade options, the West and the Maritimes strongly supported broad bilateral free trade and urged the Government to move rapidly to negotiations. The West expressed concern that the "window of opportunity" would close unless Canada took an early initiative. It stressed the importance of trade opportunities in the rapidly growing Pacific Rim markets and emphasized that Canadian trade restrictions affecting these countries would harm our export potential.

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* This report was prepared following Minister Kelleher's initial, extensive, Canada-wide consultations concluded at the end of May, 1985.

In the Atlantic provinces, many expressed strong concern regarding U.S. contingency protection measures as they affect lumber, agriculture and fisheries, as well as "Buy America" procurement provisions. They also addressed problems of single-industry communities and regions and higher labour costs confronted by Canadian manufacturers.

In Quebec, the consultations in Montreal echoed the broad support heard in the Western and Atlantic provinces for early negotiation of a comprehensive trade agreement, including from representatives of the clothing and textile sectors. In contrast, in Quebec City such views were muted by concerns of small businessmen over the adjustment impact of increased import competition. The Quebec Chamber of Commerce submitted a detailed written brief favoring a comprehensive trade agreement with the United States.

In Ontario, the response was more cautious. Whereas the majority view strongly favoured broad trade liberalization and better discipline on non-tariff measures, it was also emphasized that action on inter-provincial trade barriers must be integral to this process. Serious doubts were expressed by some on the ability of Canadian industry to compete with the United States, given higher costs notably of labour, smaller plants and a heavy degree of foreign ownership, leading to the hypothesis that some firms might disinvest in Canada under a liberalized trade regime.

Consultations with business highlighted the importance of seeking improved access to export markets for Canadian primary agriculture, fisheries, resource- and energy-based products as well as for a broad range of machinery, equipment and other manufacturing products. The significance of enhancing the security and predictability of export access conditions, particularly by reducing the vulnerability to the U.S. import contingency protection system, was a major concern across the country. Particular import sensitivities appeared in the areas of agricultural and processed food products, paper products, specialty chemicals and plastics, shipbuilding and offshore drilling equipment, auto parts, furniture, textiles and clothing, footwear and cultural products. Import penetration concerns were evident in meetings with the Canadian Pulp and Paper Association as well as with the various cultural associations.

The focus of the ministerial consultations was on the U.S. market. However, some sectors, in particular agricultural, fisheries, resource products and petrochemicals also gave considerable priority to the need actively to seek offshore markets especially in the Pacific Rim and Europe.

Senior labour representatives in Vancouver, Toronto and Montreal agreed with the need for Canada to improve its competitiveness but stressed that two-thirds of Canadian market demand was domestic rather than export-oriented. The Canadian Labour Congress was particularly concerned over the employment impact of increased competition, either from newly industrialized countries or the Uunted States, and the effect bilateral and multilateral trade liberalization would have on unemployment, structural readjustment of the Canadian economy, medicare, bilingualism, social policies, health and safety regulations, and collective bargaining practices generally. Labour tended to argue in favour of investment and job protection provisions so as to ensure "good, secure, well-paying jobs at home and not just entrepreneurial access". It also argued that the flow of technology must be intrinsic to any negotiation to ensure that Canadian industrial capacity did not become obsolete. Attention was also drawn to the importance of trade in services as labour perceived future job creation to lie predominantly in the services area.

PROVINCIAL GOVERNMENT ATTITUDES

Provincial governments strongly urged the federal government to take early initiatives to secure and improve Canadian exports to the U.S. and to work toward a new MTN at an early date to further their global market interests. The Regina First Ministers' Conference supported multilateral negotiations and movement towards a process of negotiation with the U.S. but with prudence. On May 28, Federal-Provincial Trade Ministers agreed that there is "an urgent need for a comprehensive agreement to secure and expand our access to the U.S. market". The Ministers also recognized that any negotiations should be based on mutual advantage. Provinces generally felt that sectoral studies would be crucial, that impact studies should be accelerated, that studies should be shared and that provinces should participate actively in the preparatory and negotiating phases. They also argued in favour of transition periods for sensitive sectors and a clear commitment to adjustment measures when necessary and where appropriate.

Whereas Quebec, as well as the Western and Atlantic provincial governments desired to see the federal government proceed with negotiations on a comprehensive trade agreement with the United States as soon as possible, the Ontario government was more cautious in its approach. Ontario's concerns focussed on import surges in high technology, possible disinvestment in

Canadian industry, the employment impact and U.S. pressures for harmonization in other areas of economic and social policy. It considered that non-trade policies would need to be addressed, including interprovincial barriers, R&D tax incentives and the promotion of global product mandating. Manitoba's support for exploration of a comprehensive agreement was "conditional upon an extensive period of adjustment being provided for industry sectors and workers adversely affected".

The four Western Premiers at their mid-May meeting in Grande Prairie, joined in supporting a proposal to examine the benefits and disadvantages of a comprehensive Canada-U.S. trade liberalization agreement, provided there was full provincial participation in all stages of negotiations and conditional upon adequate adjustment measures for adversely affected workers and industrial sectors. They also reaffirmed their interest in a new MTN, and outlined their objectives emphasizing both the importance of the U.S. and the Asia-Pacific area. Premier Lougheed of Alberta had visited Washington D.C. in early May. He provided a first-hand report to the Prime Minister in a letter of May 14 in which he urged the government "to initiate a new and comprehensive bilateral free-trade agreement with the United States" and signal its intention by mid-September, or "the opportunity will probably be lost for many years".

The Minister for International Trade's suggestions for provincial involvement in the preparatory phase were accepted, namely the establishment of single focal points in Ottawa and the provinces to ensure ongoing two-way communication, meetings of federal and provincial officials in June, July and September, 1985 and meetings with individual provinces on request. The question of provincial involvement in negotiations themselves was set aside until such time as decisions were taken to actually proceed to negotiations.

> **Canadian policies are almost never directed against the United States or its interests. They are directed toward strengthening a country of middle rank, not yet fully industrialized and competing with difficulty with both much larger and more integrated economies and much smaller and less costly ones.**
>
> **Gordon Robertson, "The United States and Problems of Canadian Federalism," In Canada and the United States: Enduring Friendship, Persistent Stress. Edited by Charles F. Doran & John H. Sigler.**

Ottawa

June 28, 1985

CANADA-UNITED STATES TRADE NEGOTIATIONS: THE ELEMENTS INVOLVED*

INTRODUCTION

Canada is a trading nation. Much of our economic structure can be explained only in terms of our external trade. More than thirty percent of Canada's GNP is generated by our exports of goods and services. At the same time, Canada imports a wide variety of both producer and consumer goods which either cannot be produced in Canada or which can be obtained more cheaply from abroad. Massive capital developments have taken place to serve foreign markets. Few countries are as visibly dependent on external trade for the development of their economy as is Canada. Canada does not possess a large internal market, nor does it have preferred access to a larger market through a regional trading bloc. As a first rank producer of commodities like nickel, wheat, and uranium, and as a manufacturing nation, highly skilled in the production of aircraft, automobiles and nuclear power plants, as a major force in world banking and consulting engineering, its prosperity depends on its ability to sell goods and services in many parts of the world, especially in the United States, Western Europe and Japan. Furthermore, Canadians have become dependent on imports of a wide range of both producer and consumer goods to satisfy basic demands at the best possible price. Trade is thus a key factor in the efficient development of the Canadian economy and the maintenance of a high standard of living for Canadians.

The government in January issued a Discussion Paper, *How to Secure and Enhance Canadian Access to Markets*, which provided an initial focus for discussion, consultation and debate on the government's approach to trade policy. During these consultations, there appeared to be clear evidence of interest in Canada for movement to a process of trade negotiation with the United States. The commitments set out in the Quebec Trade Declaration to give the highest priority to finding mutually acceptable means to reduce and eliminate existing barriers to trade in order to secure and facilitate trade and investment flows provided a basis for the government to continue its trade policy consultations. Throughout these consultations, the government's intent has been to provide a sound basis for a decision on an approach to secure and enhance access to U.S. markets.

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* This paper was prepared in June 1985 as a guide for the analytical work which helped to lay the foundation for the government's September decision.

The United States Administration has indicated it supports a bilateral approach: both trade and economic policy and wider foreign policy objectives for the United States underpin this attitude. From the U.S. perspective, a stable Canadian economy meets U.S. foreign, trade and macro-economic interests. But the U.S. has indicated that any overtures would of necessity have to come from Canada; we have the most at stake. The evolving United States attitude has been clearly demonstrated in its willingness to deal with its trading partners on a bilateral basis through new trading arrangements with Caribbean countries and Israel.

While advocates and critics of a trade agreement with the United States frequently characterize the issue as one of free trade, it is both much more and much less. The economic concept of free trade, i.e., trade which is unfettered by government-imposed trade restrictions, is unlikely ever to be achieved between two sovereign countries. Indeed, it does not now exist among Canada's ten provinces after 120 years of economic union. Thus, freer trade between Canada and the United States would always be less than what the economists have traditionally envisaged. But in today's context it should be more than the removal of tariff barriers. Even were tariffs to be removed, trade would not be free because of the many other types of barriers governments have devised. Future negotiations, therefore, would need to address more than tariffs.

A further important consideration to be kept in mind is that future negotiations would be both ways. In order to gain something of value, we would have to give something of value. It would be naïve to think that a comprehensive trade agreement will secure and enhance our market access without making reciprocal commitments on access to the Canadian market. In order to achieve our objectives, therefore, we would have to face hard choices and be prepared to make trade-offs.

OBJECTIVES

For Canadian producers and investors, the test of our foreign trade policy lies in whether the government can successfully improve market access for those sectors where Canadian production is or can be competitive in world markets and whether it can maintain current access available to Canadian producers. Private sector investment is a key to growth and job creation. Canadian producers need to be confident that their market access is secure and that foreign governments will not move to frustrate the effort of Canadians to market their goods abroad.

Broadly stated, therefore, Canada's objectives in any trade negotiation would include the following:

- a more ordered world trading environment, promoted by the introduction of sufficient stability, predictability and transparency in international trade relations to inspire business confidence and thus lead to job-creating investment;
- more secure access to major markets, particularly the United States market;
- more discipline on the trade-distorting practices of our major trading partners;
- improved opportunity for the further processing of our natural resources before export, by reducing or eliminating barriers to manufactured goods;
- improved access and trading conditions for agricultural and fishery products;
- scope to protect Canadian producers against injurious and unfair import competition equivalent to that available to their foreign competitors; and
- an improved framework of rules that will encourage orderly adjustment in the Canadian economy.

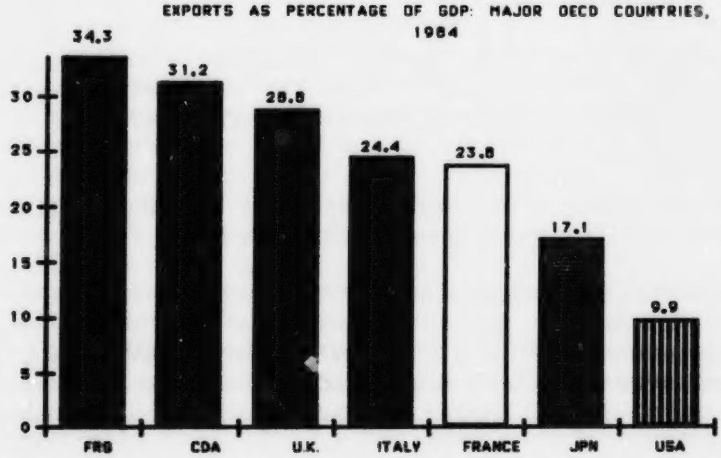
More particularly for the United States market, Canada's objectives would be to instill a trade and investment climate which could contribute directly and positively to the creation of more and better employment opportunities. This would involve:

- security of access to that market particularly by reducing the risks inherent in the U.S. system of contingency protection;
- better access to world-class technology;
- unimpeded access to the U.S. market in order to provide Canadian industry with a sufficiently large market base to realize economies of scale and specialization and to carve out niches for specialty products; and
- a stable North American trading system which would induce a substantial but orderly adjustment in Canada towards a more competitive economy, providing an increased incentive for investment from all sources.

Over the past forty years, Canada has pursued its trade objectives primarily through multilateral negotiations, supplementing these where necessary with complementary bilateral agreements. These objectives, however, can in today's circumstances also be pursued through bilateral mechanisms, especially with our most important trading partner. The advantage of the bilateral approach is that we can pursue more directly the most pressing problems between us. It is also the only way we can gain special exemptions. The bilateral approach allows both countries to open their borders to an extent neither may be willing to do immediately for third countries. The two types of negotiations should be seen as complementary and mutually reinforcing, with the one primarily geared to general, world-wide objectives and the other to unique bilateral concerns.

We can't, however, have it both ways, i.e., use the multilateral system where it suits us and then seek exemptions and special deals where it doesn't. A comprehensive trade agreement, therefore, should be consistent with our multilateral obligations if we wish to continue to reap the benefits of GATT membership.

CHART 2



WHAT WOULD BE INVOLVED IN A TRADE AGREEMENT

A comprehensive Canada-United States trade agreement should be capable both of shielding us from the effects of protectionist measures and of increasing our access to our most important market and thus provide a base for instilling greater efficiency into our economy. It should be more extensive than what was sought by Israel. Unlike them, we attach considerable importance to gaining a better handle on contingency protection. A comprehensive agreement would involve a substantial reduction in tariff and non-tariff barriers on a bilateral basis. It would be the logical extension of the political commitments entered into at Quebec City to seek to facilitate cross-border trade flows. Such an agreement would be more extensive than a framework agreement and be more comprehensive than either sectoral or functional agreements. Agreements of similar scope and content have been negotiated between the U.K. and Ireland, between New Zealand and Australia and between the individual countries forming the European Free Trade Association (EFTA) and the European Communities.

A comprehensive Canada-United States Agreement would be similar to that between Australia and New Zealand but the extent of trade and other economic flows between Canada and the United States is unique, and an agreement between us would have to recognize this uniqueness. Such an agreement, however, would not be as extensive as a customs union or a common market. The latter two require a much higher degree of economic integration and harmonization of economic policy than would be required by a comprehensive agreement of the kind contemplated by Canada. A customs union, for example, would require that the two countries maintain common barriers to third country imports while a common market in addition would require the free movement of capital and labour.

The GATT agreed from the outset that participants could negotiate agreements limited to a few members. Such an agreement must meet a number of criteria, the most important of which is that it should aim to increase trade rather than divert it. The criteria are set out in Article XXIV of the General Agreement. GATT requires that "restrictive regulations of commerce are eliminated on substantially all the trade between the constituent territories." While present projections suggest that up to 70% of Canada's exports will enter the United States free of duty after 1987, more than duty-free treatment is required to qualify. It must include other restrictive regulations of commerce such as quotas, anti-dumping and countervailing duties and standards.

An agreement negotiated pursuant to Article XXIV is not subject to GATT approval, but rather is examined for consistency by GATT members. If GATT members conclude that the agreement is not consistent with Article XXIV, they make recommendations to the parties involved who are expected to heed their recommendations. Working parties established to examine the EC and EFTA agreements have never been able to agree as to whether these agreements are consistent with Article XXIV. As an historical matter, therefore, the GATT has never approved or disapproved of any Article XXIV agreements.

As a working hypothesis, therefore, this paper proceeds on the analytical assumption that the objectives outlined above could be pursued by a comprehensive trade agreement negotiated concurrently with active participation in the preparation for new multilateral trade negotiations. Described below are the kinds of issues that need to be addressed in order to arrive at a clear understanding of what would be involved in such a trade arrangement with the United States. The issues described are those consistent with an Article XXIV agreement as defined in GATT.

NATURE OF A COMPREHENSIVE AGREEMENT

I. Product Coverage and Scope

The first order of business is to come to some working hypothesis as to how comprehensive any bilateral agreement would need to be. Preliminary analysis based on the 1983 sectoral initiative, the experience of others and the requirements of GATT suggests that the approach most likely to accomplish our objectives would be to cover all product areas but allow for either temporary or permanent opting out of certain product lines or even sectors. Macro-economic analysis suggests the greater the coverage, the greater the potential benefit to the economy.

Particular attention will need to be given to those sectors traditionally considered to be sensitive with a view to determining whether special transitional treatment or exemptions would be warranted. Experience under GATT suggests that some sectors can be treated differentially. For example, if it can be clearly demonstrated that the respective domestic regimes for a sector in place in the two countries are sufficiently different to make the removal of barriers extremely complicated or impractical, the removal of barriers can be delayed.

An important area of choice is whether any arrangement should be limited to trade in goods or include trade in services. Given the vastly different experience in international law and practice for the two areas, even if services were included, consideration needs to be given as to whether a separate regime for services would be required. Services are not now covered by GATT disciplines and thus coverage of services would largely break new ground.

Recognizing the need for trade-offs within or between individual sectors, preliminary profiles were developed to gauge the probable impact of a comprehensive agreement on various sectors. These profiles will be further developed and refined in consultation with business, labour, the provinces and other interests. It should be recognized, however, that profiles can be no more than indicative in nature. No amount of analysis can predict with precision what would in fact happen as a result of a comprehensive agreement. The most important objective would be to seek a net increase in the quality and quantity of employment in the medium-term.

2. Barriers to be Addressed

Trade can be impeded in a number of ways. A comprehensive trade agreement would need to come to grips with most of these if it is to meet the above objectives. In general, an agreement should aim to enshrine the principle of national treatment, i.e., that the products of the one country are treated in like manner to the products of the other. Among the most important barriers would be the following:

- **Tariffs** - The tariff on many products traded between Canada and the United States is already at zero. An agreement should aim at eliminating all other tariffs over an agreed period of time, with phasing and transitional arrangements tailored to the needs of the sectors covered and reflecting the asymmetry between the scale of production in the U.S. and Canadian economies.

- **Anti-dumping Duties** - anti-dumping duties can be charged in instances where imports are priced at less than the "normal" prices charged in the exporter's domestic market and cause material injury to domestic industry in the importing country. Since dumping is frequently a product of a country's own tariff barriers, dumping would probably occur less frequently under duty-free trade conditions. Nevertheless, agreement would need to be reached on how to deal with dumped goods as well as to avoid diversion of dumped products from third countries. While competition law in both jurisdictions could be used as a substitute, fair trade rules and the relatively greater exposure of Canadian production to U.S. import competition could require the retention of some form of anti-dumping procedures. One option for consideration would be the development of a separate bilateral regime.

° **Subsidies and Countervailing Duties** - Countervailing duties may be imposed when subsidized imports cause material injury, such as reduced sales and profits and employment losses to domestic industry. The problem is especially acute for Canada given the fact that more than half of a plant's production is often destined for the U.S. market, whereas it is rare for more than 10% of a U.S. plant's production to be destined for Canada. The threat of countervail has proven to be a major deterrent to investment in Canada. Essentially, Canada's concern is to determine what we are prepared to accept regarding government regional and industrial assistance programs so as to reduce the risk of countervail while preserving our ability to use such measures in pursuit of national goals. This issue lies at the heart of the concerns of the business community.

° **Safeguards** - Safeguards are those measures, such as additional duties or quotas, which governments from time to time impose to restrict fairly traded imports which nevertheless cause or threaten serious injury to domestic producers. The complete dismantling of safeguard or escape clause provisions may be desirable, although some would argue that it is more reasonable to assume that such a provision would continue to be necessary in both countries. In order to provide the predictability and assurance of access that would be in keeping with freer trading conditions, it will be necessary to determine how safeguard actions involving each other can be reasonably circumscribed and how to treat each other's exports in the case of measures aimed primarily at others.

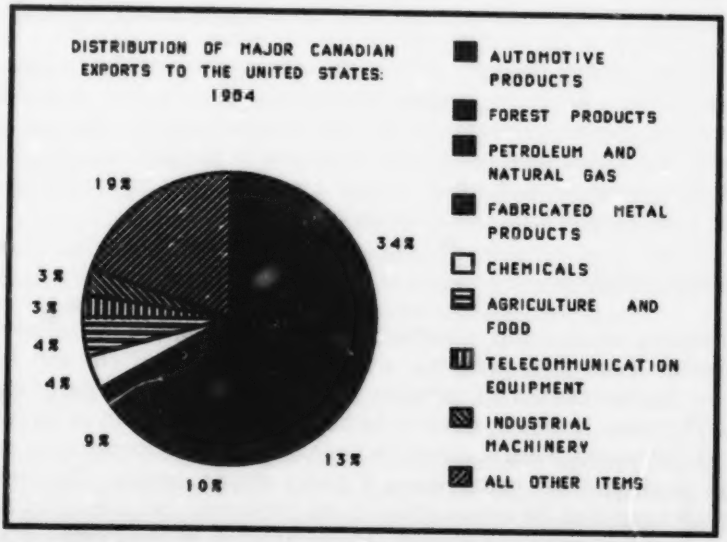
° **Balance-of-Payment and National Security Restrictions** Balance-of-payment restrictions usually take the form of temporary, across-the-board import restrictions or surcharges to correct severe imbalances in international payments. Canada imposed such restrictions in 1962. The introduction of a 10% surcharge by the U.S. in 1971 had serious repercussions on Canada. That experience suggests the need to come to an understanding on this issue.

° **Government Procurement** - Only a relatively small proportion of purchases by governments in Canada and the United States now takes place under fully competitive circumstances. The Quebec Declaration has laid the basis for exploring the feasibility of extending national treatment to each other's products in government purchases. The size of the North American procurement market, when account is taken of state and provincial procurement, has been estimated to be as high as $500 billion a year, of which less than 10% is covered by the GATT procurement code. Of particular interest to Canada is gaining access to U.S. federally funded programs, such as the Surface Transportation Assistance Act, access to which is limited by Buy America restrictions. U.S. interest is likely to focus on provincial procurement.

- **Other Non-tariff Measures** - in addition to the above barriers, there are other policy instruments which have a direct or indirect trade inhibiting effect, such as standards, patent law, copyright, licensing, etc. These could be addressed, for example, through harmonizing national practice and/or developing codes of conduct under a comprehensive trade agreement.

Generally, effective control or elimination of these barriers would improve and secure Canadian access to the U.S. market and thus provide access to a sufficiently large market to realize economies of scale and specialization as well as the kind of stability Canadian manufacturers need to engage in long-term structural adjustment to world-wide competitive pressures.

CHART 3



3. Technical Issues

Movement towards barrier-free trade would require the development of a number of provisions now not prominent in Canadian or U.S. trade law but which would be necessary to effect the new trading conditions. The most important of these would be rules of origin, i.e., ways and means to differentiate

Canadian and U.S. origin goods from those imported from third countries. Without such a provision, imports from third countries would tend to enter the country which has the lower barriers to third-country imports and thus move to the other country. Current U.S. and Canadian rules are substantially different. Consideration would also need to be given as to how to administer special import and export provisions applied to third countries.

4. Investment

While not a prominent feature in other trade agreements, the high-level of U.S. investment in Canada and the growing level of Canadian investment in the United States suggests that some consideration will need to be given as to whether or not any special rules are needed to safeguard investment, how to deal with multinational companies, whether trade-related investment issues need to be addressed, etc. Such consideration would be designed to provide long-term stability.

5. Adjustment/Transition

Any major change in the trading regime would require adjustment by industry on both sides of the border. Given the asymmetry of the relationship, adjustment would likely be greater in Canada than in the United States. Consideration, therefore, would need to be given to developing special transitional and adjustment assistance measures to smooth out adjustment to changed circumstances and which would not be subject to the discipline of contingency protection for a specified period of time.

6. Harmonization

A closer trading relationship, whether or not achieved within the framework of formal institutional arrangements, would bring pressures for and increase interest in harmonization of policies and even legislation, particularly in Canada. The issue, however, needs to be kept in perspective. In an increasingly interdependent world, there is already a large degree of harmonization, not only between Canada and the United States, but with other countries. The pressure is not so much a result of the nature of any trade agreement, but a result of the need to compete, both at home and abroad. Harmonization in some areas, of course, would be beneficial, while others would be harmful to maintaining the integrity of the Canadian nation. Furthermore, the Quebec Declaration specifically recognizes this phenomenon and calls for consideration of ways and means to standardize, reduce or simplify regulatory requirements.

7. Institutional Issues

Any major trade agreement would require sufficient institutional mechanisms to provide for its effective management and for the rapid and equitable settlement of disputes. The shape and scope of such mechanisms would be largely determined by the coverage of the agreement. The more comprehensive the agreement, the more extensive would be the need for management and the potential for dispute. It would require provision for consultation and review, dispute settlement, and the identification of responsible national officials to undertake various tasks.

8. International Obligations

In addition to GATT, Canada and the United States are both parties to various international treaties and arrangements in the trade field. Any new comprehensive arrangement would affect and be affected by existing obligations.

9. Impact on Third Countries

While Canada and the United States are each other's most important trading partners, both countries trade with many other countries and have economic interests all over the world. The overall objective should be trade-creating, and refrain from any measure than would limit current opportunities in the North American market for third-country suppliers. The improved and more secure access which Canadian producers achieve in the most lucrative market in the world will influence their competitive ability in other markets. The government has already taken a series of measures to enhance Canadian presence in other markets especially the fast growing countries of the Pacific Rim.

COSTS AND BENEFITS

If the government decides to proceed, a comprehensive agreement as described above should aim at increasing the security of our access to our most important market, a condition essential for growth and new investment given the relatively small domestic Canadian market. It should also improve the existing access we enjoy in the U.S. market and thus allow Canadian industries now shut out of that market, to grow and invest with renewed confidence. Finally, it should increase the competitiveness of our manufacturing sector by encouraging a process of restructuring and rationalization of Canadian industry to serve the North American market and, from that base, to penetrate overseas markets.

Many studies and commentaries have been published in recent years attempting to show the impact of Canada-U.S. trade liberalization. Primarily undertaken by academics, these studies assume, virtually without exception, the total elimination of both tariffs and non-tariff barriers. In addition, the Macdonald Commission has commissioned some 40 studies which touch directly or indirectly on Canada-U.S. trade relations.

As part of its own work program, the Department of External Affairs commissioned the Institute for Research on Public Policy to do a survey of the existing literature on this subject. The following is a synopsis of that survey. The macroeconomic studies show that:

- the economy should grow from 3 to 8% through economies of scale and specialization resulting from secure access to a large market;
- exports should grow;
- productivity should increase with the results that the present 25 to 30% productivity gap between Canada and the United States should close;
- employment should rise across the Canadian economy as a whole in both manufacturing and services and more so in the latter;
- average income should increase as a result of the projected improvement in the efficiency of the Canadian economy; and
- consumers should benefit from lower prices on consumer goods and from greater variety in choice.

The studies further suggest that:

- resource sectors will gain;
- manufacturing industries that are capital intensive e.g., transportation equipment, chemicals and paper products should prosper while those that are labour intensive e.g., leather, furniture and small electrical appliances would need to adjust; and
- all regions of the country gain. All studies confirm that Ontario will be the greatest net beneficiary;

However, these studies must be recognized for what they are. They are largely theoretical and based on historical data. They provide, in extremely general terms, a sense of direction in which the economy would go, were tariffs and non-tariff barriers eliminated and all other factors to remain as they are now. These studies do not, and cannot, serve as a guide to negotiations with the United States because they assume an agreement the details of which have yet to be negotiated. Any trade agreement would, of course, need to be negotiated and would thus also need to meet U.S. trade objectives. In other words, negotiations would be two-way and not without reciprocal commitments from Canada.

In addition, an agreement would have to be pursued and implemented in such a manner as to minimize the normal side effects of any form of trade liberalization. For example, adjustment would need to be made to new circumstances. Adjustment, of course, is an ongoing process which will affect Canadians whether we move to freer trade or not. It will involve some sectors growing, while others decline. This process of expansion and contraction will most directly affect labour.

The possible employment effect of Canada-United States trade negotiations has and is likely to continue to excite interest and controversy. The government's overall objective, however, should be to save jobs threatened by U.S. protectionist measures in the short term and to stimulate more and better jobs in the medium to longer term. Serious methodological problems do not permit an exact estimate of the impact on employment. The experience of previous trade negotiations, however, clearly demonstrates that trade liberalization has positive employment effects.

The only major theoretical study of employment effects resulting from trade liberalization in Canada is that done by Rick Harris of Queen's University, in cooperation with David Cox of the University of Western Ontario. Based on a new model developed specifically for studying trade effects on the Canadian economy, Harris has run a number of experiments aimed at estimating the employment effect of unilateral free trade, multilateral free trade, bilateral sectoral free trade and general bilateral free trade. All these experiments resulted in estimates of positive employment effects, i.e., an increase in aggregate numbers employed and intersectoral movement from low-paying jobs in weak sectors to better-paying jobs in stronger sectors resulting from trade-induced growth in strong sectors and retrenchment in weak sectors.

In a study prepared for the Macdonald Commission comparing the results of sectoral and general bilateral free trade, Harris estimates that under bilateral free trade, employment would increase by 5% within two years of an agreement's implementation and that up to 7% of the labour force may need to shift employment from one sector to another.

The study has been criticized by some specialists, largely due to the assumptions and data used. There is, however, broad agreement that it is the best available model for this type of theoretical study. The government, therefore, through the Department of Finance, is working with Messrs. Cox and Harris to fine-tune the assumptions and provide the best possible data. Once this project is completed, a number of new theoretical experiments will be run in an effort to develop more accurate results.

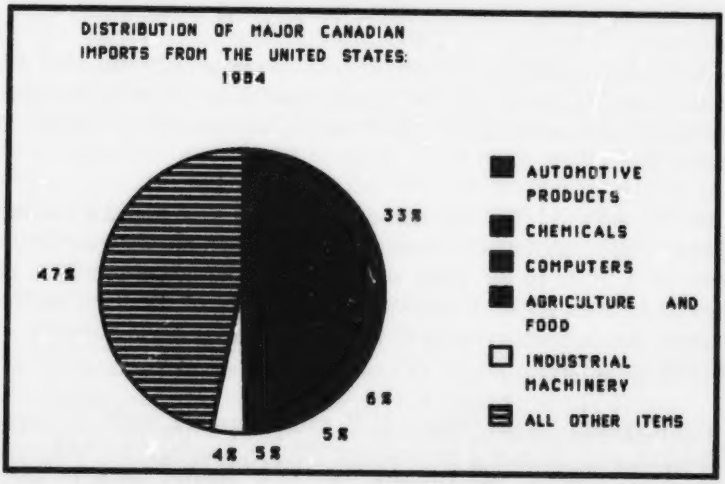
No amount of analysis can predict with exactitude, however, what will happen, but, on the basis of the majority of studies done by academics and research institutions, it is clear that long-term gains will be substantially greater than short-term adjustment. Such adjustment, moreover, can be cushioned by the introduction of appropriate assistance measures. The inclusion of service sectors, where there is less experience, would make forecasting even more difficult.

While the negotiation of a comprehensive trade agreement will be a major undertaking and affect the country in many ways, it should also be kept in perspective. The costs should not be excessive and result in large-scale transfers of labour between sectors of the Canadian economy, with consequent large increases in unemployment, as has been suggested by some. Such a spectre is not credible, although adjustment may be difficult in some smaller centres. Freer trade would affect mainly manufacturing industry in the Canadian economy, and manufacturing accounts for some 20 percent of employment in Canada. Given the adjustments already made to previous trade negotiations, at most, freer trade would have direct effects on only a small percentage of the labour force. Furthermore, experience following previous major trade negotiations suggests that most of the adjustment will be within industries, rather than between industries, and at a quicker and more positive pace and level than anticipated. Neither the costs nor the benefits should thus be exaggerated.

A review of the political sovereignty implications of a move toward freer trade should also convince us that there are benefits. It should strengthen the economic fabric of the country; it should reduce regional differences on the conduct of trade policy; and it should reinforce a growing sense of national confidence. Given the reality of our close economic relationship with the United States, a bilateral treaty could be a better guarantor of our sovereignty than the gradual uncontrolled drift toward integration now taking place. The possible adverse consequences can be managed by pursuing deliberate policies of strengthening cultural and other fields of endeavour which would bolster our national identity.

It is an exaggeration to claim that economic cooperation and rationalization lead inevitably to political integration and absorption. Persuasive examples that this is not the case are afforded by the free-trade arrangements that have been forged, on an individual basis, between the European Communities and the countries of the European Free Trade Association (EFTA), Norway, Sweden, Finland, Iceland, Portugal, Austria and Switzerland. None have populations in excess of 10 million as compared to an EC population of 250 million. Yet no one would suggest that these countries have lost their distinctiveness or felt constrained to mirror the EC in their foreign policy or other areas of endeavour. There certainly has been no effort to effect political integration. Similarly, the free-trade arrangement between the U.K. and Ireland, before they both joined the Community, did not dispose the Irish to become more like the British, nor have we seen any evidence that New Zealanders are becoming more like Australians as a result of their bilateral free-trade agreement. While no two situations are ever exactly alike, there is no historical precedent of freer trade leading inevitably and unwillingly to political absorption.

CHART 4



AMERICAN ATTITUDES

The current U.S. authority for bilateral trade negotiations can be found in the 1974 *Trade Act* and the 1984 *Trade and Tariffs Act*. It requires the Administration to seek opportunities for U.S. exporters equivalent to those afforded to foreign exporters, i.e., to arrive at balanced agreements extending mutually advantageous commercial and economic benefits. The United States has tested this authority in negotiations with Israel and Caribbean countries.

The U.S. interest in freer bilateral trade with Canada is neither casual nor recent. Better and more secure access to its most important market, now accounting for C$65 billion in exports, is not to be taken lightly. The U.S. welcomed the federal government's sectoral initiative in 1983, although both sides have since agreed that the scope for bilateral liberalization on a sectoral basis is limited.

A firm expression of U.S. interest was demonstrated in the Declaration on Trade issued by Prime Minister Mulroney and President Reagan at the end of their March 17-18, 1985 meeting in Quebec City. In that document, the two leaders made a strong political commitment to consider all available means to liberalize trade between the two countries. As an indication of the seriousness of their interest, they adopted a specific work program and schedule to negotiate a number of specific agreements to reduce barriers to the freer flow of trade and investment, while the two governments consider whether to take the broader step. The interest of the Administration, therefore, is clear.

The United States could be expected to have priority objectives for a bilateral agreement reflecting the issues the Administration has cited as irritants on the trade agenda as well as those for which the United States is pressing for clearer international disciplines, such as:

- **tariffs** - the U.S. would find of interest a substantial reduction or elimination of tariffs. The level of the Canadian tariff on dutiable imports from the U.S. is in the order of 9 to 15% with some products attracting rates as high as 25%. Elimination, especially of the high tariffs, would increase the competitiveness of US producers vis-à-vis domestic and third country suppliers.

- **contingency protection** - U.S. producers are more concerned with Canadian anti-dumping procedures than our safeguard and countervail procedures. More importantly, the U.S. would wish to see greater discipline on Canadian subsidy practice in return for reduced opportunity for resort to countervail by U.S. producers.

- **investment** - the U.S. may seek acceptance of contractual commitments on the treatment extended to U.S. investors once established in Canada and greater discipline on trade-related investment measures.

° **services** - the U.S. would attach priority to the negotiation of a framework of rules to cover traded services. The U.S. interest in negotiating such a framework agreement relates not only to the specific issues to be negotiated, but also to the demonstration effect such a negotiation with a major trading partner would hold for multilateral or other bilateral negotiations.

° **government procurement** - the U.S. would be reluctant to extend national treatment in government procurement unless Canada extended reciprocal and contractually binding commitments to federal and provincial procurement.

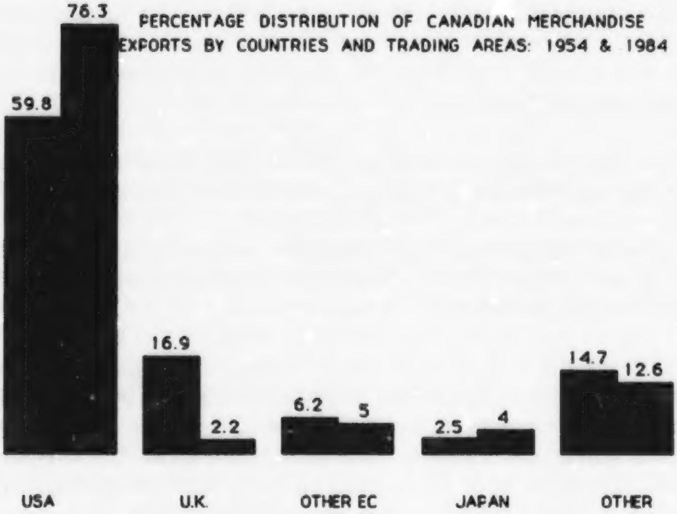
° **intellectual property** - the U.S. has long identified counterfeit, patent and copyright law as requiring greater international discipline.

° **provincial practices** - in addition to procurement, the U.S. would likely seek greater discipline on provincial practices related to resources, liquor boards and some services.

The attitude of the Congress is more complex. While the Administration generally favours freer trade, the Congress, influenced by individual lobbyists and interest groups, tends to be biased towards protection or bilateral trade agreements where the trade-offs are more clearly visible. While there are individual Senators and Congressmen who have expressed support for Canada-U.S. bilateral negotiations, the attitudes of the Congress in general would be much influenced by the interests of the U.S. business community and the sectoral costs and benefits individual businessmen see. This is not all that different from what exists in Canada.

> **The effects of freer trade would be confined largely to secondary manufacturing industries. But there is now extensive evidence to suggest that only rarely would the dropping of import barriers result in the displacement of whole industries by foreign competition.**
>
> **In the great majority of instances, what would be expected is a shift to more specialized lines of production within industries. This is exactly what occurred under trade liberalization in the EEC, EFTA, and other free trade arrangements.**
>
> **Economic Council of Canada, An Outline of a New Trade Strategy for Canada, 1975**

CHART 5



" By acting boldly to establish a new and more stable relationship with the United States, Canadians could begin to relieve themselves of that corrosive feeling of inferiority and could free their energies to solve those problems that are under national jurisdiction."

Anthony Westell, "Economic Integration with the USA."

MULTILATERAL TRADE NEGOTIATIONS: SOME INITIAL CANADIAN VIEWS

1. Canada regards the new Multilateral Trade Negotiations (MTN) as both a challenge and an opportunity to find forward-looking solutions to the current and emerging problems facing the international trading community. Canada is approaching the MTN with a sense of urgency and importance to fight protectionist threats, to enhance the rule of law in international trade and to restore the momentum towards further trade liberalization.

2. With an economy highly dependent on international trade, Canada attaches a high priority to a further opening of national markets to international competition and to dealing with market access and trade related issues which have an adverse impact on the prospects for new productive investments in internationally competitive industries. To the extent Canada is able to expand access to international markets it will be prepared to make its contribution to enhancing a more efficient international allocation of resources and to facilitate the necessary structural adjustments.

3. The MTN will provide an opportunity to enhance Canada's economic cooperation and trading relationships with developing countries within the multilateral framework. Canada is convinced that the new MTN can significantly advance the trade and economic development interests of developing countries. The benefits which the more industrially advanced developing countries derive from open world markets are undeniable as are the risks that these channels may be gradually closed.

4. The negotiations should cover products in all sectors, the full array of non-tariff and tariff measures as well as trade in service issues. A major focus should be on the strengthening of the institutional framework of the multilateral trading system and on the ways and means of securing the value of negotiated market access conditions. At this stage, Canada considers that no sector nor issue be excluded from the scope of the negotiations.

5. Canada wants to underline the importance it attaches to the Work Programme undertaken by the GATT Contracting Parties to reflect the priorities established by the Ministerial Declaration of 1982. In Canada's view, however, various elements of this Work Programme are unlikely to be brought to a satisfactory conclusion outside of the context of the new round of negotiations. Bringing the Work Programme to a satisfactory conclusion should thus be a high priority of the new negotiations.

6. The following paragraphs give a general indication of Canada's initial approach and attitudes on the main questions which, in its view, should be included on the MTN agenda and set out Canada's preliminary overall objectives and priorities in the negotiations. These objectives and priorities primarily reflect a desire to: halt protectionism and seek further expansion of access to markets; develop new rules of conduct for agricultural trade; seek tighter disciplines on the use of subsidies and on contingency protection measures; develop a framework for trade in services; and strengthen the effectiveness of the rule of law and non-discrimination governing international trade.

A. Halting Protectionism and Improving Market Access

7. The maintenance of open trading channels and the further improvement of access to export markets are vital to Canada. They are also essential elements for the intensification and strengthening of trading relationships within the multilateral trading system. Canada urges further improvement in market access conditions on as broad a basis as possible in terms of both products and markets, including in respect of customs duties. This should include the prospect of total tariff elimination in particular product areas.

8. This objective is central to restoring the confidence of the business communities in the determination and capacity of contracting parties to halt erosion of the open trading system, to reduce the risks of accelerating protectionism and to restore trade liberalization momentum. A broadly-based market opening effort would offer the prospect of significantly advancing the economic development and trade interests of both developing and developed countries.

9. Improved market access conditions in respect of agricultural and food products, fisheries, industrial resource (non-ferrous metals and forest products) and energy-based (petrochemicals) industries and related equipment and services, a range of advanced-technology and transportation equipment as well as trade in some services will be of particular Canadian interest. These sectors are still facing important barriers or trade distorting measures in Canada's major markets, for example in the form of tariffs (often still relatively high or with escalation), quantitative restrictions, restrictive government procurement practices or subsidies of various sorts.

10. A major element of market opening measures should concern the extension of the existing GATT Agreement on Government Procurement to include entities which are the main purchasers of products not now subject to international competition such as urban transit, telecommunications and power-generating and transmission equipment, as well as services contracts.

Canada would be interested in exploring the possibility of an early conclusion of the ongoing negotiations aimed at substantially enlarging the coverage of the Government Procurement Agreement.

11. Canada will be prepared to join with others in an examination of possible coordinated actions aimed at limiting special measures of protection which have been introduced in sectors facing particular international competitive difficulties.

B. Developing New Rules for Agricultural Trade

12. In the areas of agriculture, Canada will seek to bring substantially all this large area of international trade more effectively under the discipline of contractual rights and obligations and to obtain an improved balance within the framework governing agricultural trade as between all major participants. Canada will be working for the development of new, fair, predictable and effective rules on export and domestic subsidies as well as on measures such as variable levies, quantitative restrictions and export restraints.

13. These new trading rules should apply equally to all major importers and exporters and relate to third country export markets as well as import markets. They should, of course, take account of production and trade characteristics in agriculture, including the desirability of limiting the overall costs of various support programs for national treasuries. The new rules should be accompanied by the acceptance of a degree of tariff bindings more comparable to what has been achieved in respect of industrial products.

C. Tighter Discipline on Contingency Protection Measures and Subsidies

14. The benefits of trade liberalization and of tariff bindings achieved in previous negotiations risk being seriously undermined by the uncertainties associated with the use of various contingency protection measures, concerning both fair and unfair trade. There is a need to enhance the predictability of access to major world markets for producers who have sought to adjust to the substantial reduction in their protection, brought about by previous negotiations, by introducing major changes to their production facilities so as to achieve the benefits of greater specialization and economies of scale. More secure and predictable access to markets is a crucial element in order to create a reasonable degree of confidence in the business community to justify major new investments oriented to international markets.

15. The new MTN should seek to develop an integrated international understanding to bring greater discipline to the use of all forms of safeguards

actions, whether emergency import relief action under GATT Article XIX, or other measures such as voluntary export restraints and orderly marketing arrangements. This should include the question of how safeguards measures could possibly relate to undertakings on structural adjustment by the protected industries.

16. There must also be a review of existing rules concerning subsidies and countervailing measures with an aim to increase the discipline on those subsidies which are harmful to the trade interests of contracting parties, including subsidized export credits and subsidies affecting trade in agricultural products, as well as an attempt to broaden international agreement on the definition and measurement of subsidies and to improve the rules, procedures and conditions governing recourse to countervailing measures.

D. A Framework for Trade in Services

17. Given the increasing significance of services in international trade, Canada attaches considerable importance to the development of a new trading framework to provide a mutually beneficial set of rules and principles to govern trade relations in services, -- much as the GATT has done over the last decades in respect of trade in goods for the benefit of all contracting parties. This is an area where the international trading community has an opportunity to influence the elaboration of the basic rules of the road before trade in services either becomes a subject of confrontation in bilateral trade relations or the ground rules are in effect determined unilaterally by national legislation and practice.

18. The development of a new trading framework for services should, to the extent feasible and appropriate, explore the possible application of such basic principles as non-discrimination, national treatment and transparency in national regulations. The eventual status of a new instrument to govern trade in services should not be prejudged at this time.

19. Canada does not have any firm view, at this stage, as to whether the development of a new international framework for trade in services should eventually be of a comprehensive nature, whether its scope and coverage should be applicable to a selected number of sectors or whether it should be applied differently to particular sectors. Canada is flexible as to the most appropriate and practical arrangements for eventually conducting negotiations in respect of trade in services. It can accept the notion that negotiations on trade in services be conducted in parallel with negotiations on trade in goods, provided they are conducive to achieving a reasonable mutual balance of overall benefits in the global MTN context, they can be properly coordinated and the negotiation process can be appropriately serviced by the GATT Secretariat.

E. Strengthening the Effectiveness of the Rule of Law and Non-Discrimination

20. The cumulative impact of the proliferation of exceptions and deviations to the basic GATT rules over the years, and the stresses created by the strength and persistence of protectionist forces in major GATT countries are seriously undermining the credibility of the GATT itself. There are strong perceptions that the GATT is not equally respected by all its members and that it is becoming a constraint to, rather than a powerful instrument for, trade liberalization. There are also concerns that the inherent balance of rights and obligations under the GATT is being seriously altered and that it is running a serious risk of gradually becoming a less relevant instrument for dealing with new issues facing the international trading community and for managing trade relations.

21. This credibility challenge is of practical and fundamental importance for Canada because it affects the principal instrument available to Canada to preserve the achievement of past trade liberalization efforts and to manage Canada's trade relations with most other countries. It is also a collective challenge which should be met in the new MTN by seriously reviewing such fundamental questions as non-discrimination, national treatment, security of market access and dispute settlement. This should also include scope for greater Ministerial participation in and direction of GATT affairs.

F. Conduct and Management of the Negotiations

22. There are a number of considerations relating to the conduct and management of the negotiations which will need to be addressed, once the objectives of the various countries which have an interest in the negotiations are known. At this stage, it would seem appropriate to comment on a distinction which has often been made in discussions about the GATT Work Program between the so-called "traditional" issues and the "new" issues. It is not clear how useful this distinction is in practice, since the relevance of those issues for purposes of trade negotiations is how they impact on international trade flows. For instance, trade action in some of the so-called new areas such as patent infringement can have a direct prohibitive effect on the flow of goods thus placing such measures in the activity of "traditional" issues. Clearly a new round should seek to deal with all the key issues of interest to the trading countries which are expected to make a contribution to the success of the negotiations.

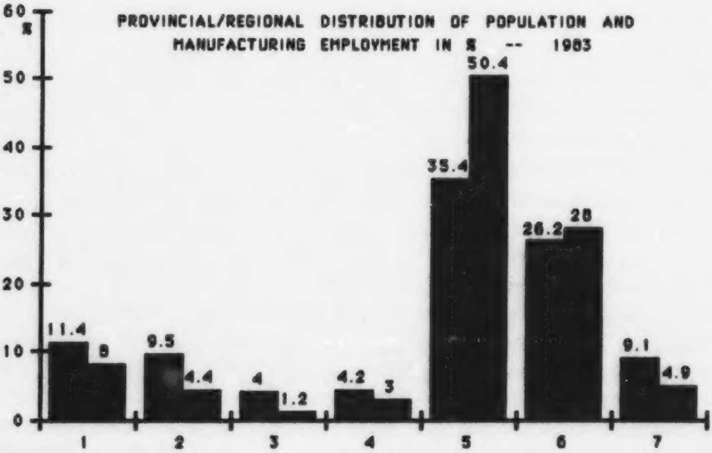
23. One important consideration concerns the relationship between trade and monetary questions, in particular the impact of exchange rate developments on trade flows. Canada supports the deployment of sustained and intensified efforts to address the problems of the international monetary system, but the

improvement in the functioning of the monetary system should not be a pre-condition for the trade negotiations nor should this be pursued within the GATT.

24. The trade negotiations should be conducted on the basis of overall reciprocity of mutual advantage. An appropriate contribution to the resolution of trade problems should be made by all participants. This contribution should be commensurate with the benefits which participants obtain from open international markets, with their economic strengths and with their interest in achieving a strengthened and more effective multilateral trading system. There should also be appropriate arrangements to allow countries having observer status in GATT to participate in the MTN if they are prepared to contribute to the achievement of the overall objectives of the negotiations.

25. Finally, Canada recognizes the importance of adhering effectively to existing commitments to ensure that contracting parties act in full conformity with GATT rules and principles. The capacity to resist protectionist pressures will clearly be a major factor in creating a favourable environment for entering into the new round. At the same time, moving diligently to launch the multilateral trade negotiations remains the most effective way of improving the prospect for contracting parties successfully fighting back protectionism.

CHART 6



LEGEND:
1. British Columbia 2. Alberta 3. Saskatchewan 4. Manitoba
5. Ontario 6. Quebec 7. Atlantic Provinces
Source: Canada West Foundation

TEXT OF CONCLUSIONS AND RECOMMENDATIONS OF THE SPECIAL JOINT PARLIAMENTARY COMMITTEE ON CANADA'S INTERNATIONAL RELATIONS

Trading Relationships -- United States

The United States and Canada have enjoyed a long and, in general, mutually beneficial trade relationship, though not without occasional periods of friction. The United States is Canada's most important trading partner and will remain so for the foreseeable future. Fully 78 per cent of Canadian exports of goods go to the United States, and 21 per cent of U.S. exports go to Canada; it is the largest two-way exchange of goods in the world. The relationship is both special and unique.

Under the terms of the GATT, and including duty-free trade under the Auto Pact and the Defence Sharing Agreement, around 80 per cent of Canada-U.S. trade will be tariff-free by 1987. Approximately 15 per cent of that trade will be subject to tariffs of 5 per cent or less. Thus, in terms of tariffs, much of Canada-U.S. trade will be 'free' by 1987.

However, a high proportion of the 80 per cent which will be tariff-free consists of commodity and resource-based products. The portion of Canadian exports to the United States that still has duties imposed on it is mostly high value-added goods produced by the manufacturing sector. It is precisely this sector of the Canadian economy that most needs to adapt to an increasingly competitive international trade environment.

There is also an extensive set of non-tariff barriers to trade between the two countries. These consist of 'standing' and 'contingent' non-tariff barriers.

Standing non-tariff barriers are government programs or regulations that tend, often as an indirect effect, to restrict trade between the two countries. Examples include government procurement policies giving some preference to domestic producers and differences in health and safety standards between the two countries.

Contingent non-tariff barriers include dumping and countervailing duties. Countries impose these either to deal with a charge of unfair trading or as part of the safeguard provisions of the GATT which permit temporary shielding of a domestic industry from foreign competition to allow it time to adapt.

Recently, there have been suggestions in some quarters in the United States that particular Canadian government programs would justify the imposition of countervailing duties and quotas. The response to such suggestions must be speedy and resolute. Such programs as Medicare, Unemployment Insurance and equalization payments do not fall within the realm of trade relations. Instead, they are essential instruments for building the equitable and just society to which Canadians want to belong and should be recognized as such by our trading partners.

Finally, the GATT regulations apply only to trade in goods and do not regulate trade in services. Services are an increasingly important component of trade between Canada and the United States and should be the subject of discussions between us.

The health of our trade relationship with the United States is of great importance to Canada. There was a strong feeling among those appearing before the Committee that this trade relationship is deteriorating, with the rise of protectionist sentiment in the United States Congress, with calls to impose import quotas on goods, and with an increasing number of countervailing duty requests being filed with the U.S. International Trade Commission and the U.S. Department of Commerce.

The Committee recommends that the government act swiftly and decisively to implement a multidimensional initiative in trade. The objectives of this initiative would be to secure our access to traditional markets, to actively develop new markets and to encourage Canadian industry to adapt to an increasingly competitive trade environment. Some of the dimensions of such a strategy would be as follows:

Mechanisms

1. Promoting a New Round of Multilateral Trade Negotiations

A successful and timely round of multilateral trade negotiations would be the most satisfactory means of dealing with Canada's trade problems. A major advantage would be that these would encompass other markets in addition to that of the United States, and these third-country markets are of considerable importance to Canada. Such negotiations would have to deal with issues not adequately covered under the GATT, such as non-tariff barriers and trade in agricultural products and services.

The government has been pressing strongly for a new round of multilateral trade negotiations. The Committee recommends that the government continue its vigorous efforts to initiate a new round of multilateral trade negotiations. The government should also address itself to the major problems that are faced by the newly industrialized countries and that relate to strengthening the international trading system, by removing international financial impediments to trade.

2. Reducing Interprovincial Trade Barriers

In consultation and co-operation with the provinces, the government should study interprovincial trade irritants and barriers and undertake an initiative to reduce interprovincial trade barriers where such barriers diminish Canada's international competitiveness.

3. Initiating Bilateral Trade Discussions with the United States

There appears to be little chance of a new GATT round being completed before 1990, and the implementation of agreements will occupy at least several years. Bilateral trade negotiations with the United States are not, however, viewed as a substitute for multilateral trade talks. Rather, the bilateral mechanism is viewed as complementary in that it affords the government the opportunity to take near-term action to deal with immediate problems. The multilateral mechanism is, by its very nature, a much longer-term process.

The Committee recommends that there be immediate bilateral trade discussions with the United States.

The discussions should centre initially on resolving current trade irritants, especially prevention of the imposition of additional non-tariff barriers to trade between the two countries. Issues such as the definition of the net effect of subsidies provided by both sides and the identification of the appropriate jurisdictional authority for implementing changes in non-tariff barriers should be dealt with explicitly. These discussions should be used to explore the potential for additional trade liberalization between the two countries and for securing and strengthening access to each other's markets. Issues such as trade in services, government procurement, and reducing remaining tariff barriers should be dealt with explicitly.

The Committee views these discussions as the natural extension of a process begun by Prime Minister Mulroney and President Reagan at Quebec City. The Committee believes that it is premature for Canada to initiate formal bilateral negotiations but that it is necessary to initiate broad discussions with the United States to determine their receptivity to liberalizing bilateral trade. After a ministerial report to Parliament on the outcome of these discussions and on whether certain conditions have been met, the government should decide whether the prospects are sufficiently promising to continue on to detailed negotiations.

The merits of several possible mechanisms for trade liberalization have been argued energetically before the Committee. These mechanisms included the sectoral, framework, and comprehensive models. There is no necessity for the Committee to recommend one of these models. Only the preliminary discussions and possible subsequent negotiations will determine how far down the road to bilateral trade liberalization we can safely travel and what the appropriate mechanisms for implementing changes will be.

The Committee feels strongly that liberalization of bilateral trade must take place within the GATT framework. In addition, the Committee would not advocate standardizing the two countries' external barriers to trade (i.e., a common trade policy with respect to trade with other countries) or complete removal of internal barriers to the movement of labour and capital between the countries. For these reasons, the Committee would not recommend that Canada enter negotiations with a view to joining either

(i) a common market, which has standardized external barriers to trade and no internal barriers to the movement of labour and capital among member countries; or

(ii) a customs union, which has standardized external barriers to trade among member countries.

The Committee believes that a bilateral trade agreement between Canada and the United States does not require exclusive concentration on the American market. It can parallel and co-exist with multilateral trade agreements and would not preclude other bilateral initiatives for trade liberalization directed at the European Community, Japan and the Pacific Rim or developing countries. A series of new bilateral initiatives may serve to stimulate movement towards a new round of multilateral trade negotiations.

The Committee recognizes that concerns will be raised as to the implications for Canadian independence and sovereignty of any move toward trade liberalization. This is clearly an area where government policy makers will have to be vigilant to ensure that distinctive cultural institutions and industries are not lost.

The Committee wishes to make several further recommendations as to the process and content of the discussions, as follows:

Ottawa Report of Parliamentary Committee August 23, 1985

1. The Committee recognizes that both Canada and the United States will want to identify exceptions to the range of subjects to be considered in any detailed bilateral negotiations. These should include policy areas and policy instruments that are of fundamental importance to the maintenance of a distinctive Canadian identity or to keeping solemn commitments made to significant elements of Canadian society. At the top of the list would be cultural industries and cultural policy, social policies, the agricultural sector and the workings of the Canada-United States Auto Pact.

The federal government has been consulting for some time with the provinces, the trade union movement, business and the farming community on bilateral trade issues. In continued consultation with these groups, the government should identify other possible exceptions to a bilateral agreement. Such exceptions could include the ability to undertake regional development initiatives. In addition, specific sectors of the economy expressed opposition to their inclusion in a comprehensive agreement. Business and trade union representatives of many manufacturing industries expressed serious concerns about the loss of their markets to U.S. competition and the associated job loss they felt would arise from a comprehensive trade agreement with the United States. Many manufacturers indicated, however, that they could adapt to the new environment if given enough time to do so.

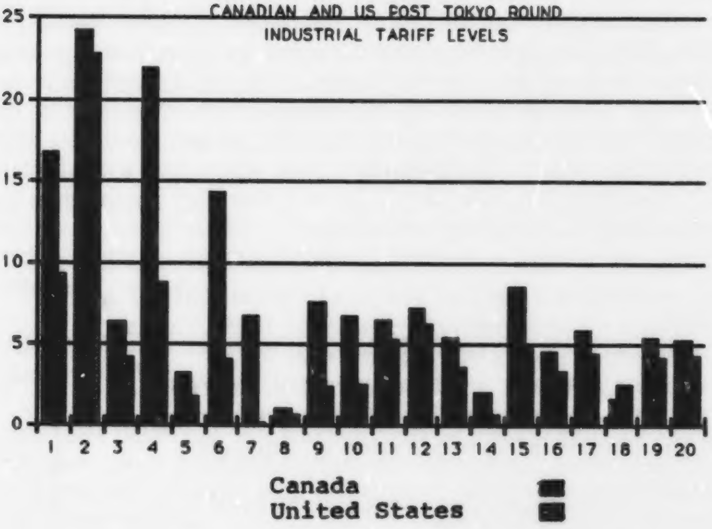
> **The recommendations of the joint Parliamentary Committee on International Relations that Canada make an immediate start on bilateral trade discussions with the U.S. is no surprise. Indeed, . . . the list of those advocating a free-trade arrangement with the Americans is impressive and growing.**
>
> **Financial Post, August 27, 1985**

Any bilateral trade agreement with the United States should contain provisions to allow time for adjustment and adaptation to take place. Such provisions would include phase-in periods for changes in trade barriers. These would be determined on a sector-by-sector basis up to a suggested maximum of 10 years. The government should examine areas of the economy that may be affected by changes in Canada's trading arrangements. There may well be a need for large-scale labour adjustment programs, to ensure that workers do not suffer from these changes, and the government should plan the financing of these programs in consultation with provincial governments, business and labour. In addition, the government may wish to use supplementary adjustment mechanisms such as an adjustment board to deal with short-term dislocation.

2. The government should perform such economic cost/benefit studies as it deems prudent prior to, and in the course of, bilateral negotiations.

3. The Committee recommends that the negotiations include the formulation of an effective mechanism for ongoing administration of any bilateral agreement or agreements, including the settlement of disputes.

CHART 7



1. Textiles
2. Wearing apparel
3. Leather products
4. Footwear
5. Wood products
6. Furniture and fixtures
7. Paper and paper products
8. Printing and publishing
9. Chemicals
10. Rubber products
11. Nonmetal mineral products
12. Glass and glass products
13. Iron and steel
14. Nonferrous metals
15. Metal products
16. Nonelectrical machinery
17. Electrical machinery
18. Transportation equipment
19. Miscellaneous manufactures
20. All industries

ROYAL COMMISSION ON THE ECONOMIC UNION AND DEVELOPMENT PROSPECTS FOR CANADA (THE MACDONALD COMMISSION)

CONCLUSIONS AND RECOMMENDATIONS

The global environment presents Canada with enormous challenges and opportunities. Rapid growth of imports from the developing countries, a changing trade-policy environment and domestic pressures on our trading partners for new protection imperil Canadian jobs. By contrast, growth and technical progress abroad offer us new export opportunities and chances to benefit from access to cheaper and higher-quality products than we can produce. As Commissioners noted at the beginning of this Part, the challenge is one of change, adaptation and adjustment; the opportunities may be unlimited. In light of these developments, however, the choices Canadians must make are difficult.

We Commissioners have been frequently reminded, in the course of our task, that Canada's domestic economy is largely defined by its relationship to the wider global economic system. Canada's last Royal Commission on our economic prospects captured this point:

> Something of Canada's essence is defined by its external relations. Much of its economic structure can be explained only in terms of its external trade...
> The ships loading lumber on Vancouver Island or aluminum ingots on the Saguenay are reminders of how deeply our material well-being is involved in the prosperity of other countries, even outside the boundaries of North America.

Canada's economic development, then, as well as our government's economic development policies, are significantly affected by conditions beyond our borders. As a relatively small, "open" economy, Canada is particularly vulnerable to outside influences on its trade and economic performance. In order to foster stability and predictability in some of these external forces, successive Canadian governments have sought to develop formal rules for conducting relationships with our trading partners. The pursuit of this objective has always involved an essential problem: How are we to reconcile conflicting priorities among national objectives and the requirements of a stable international economic system? To resolve inherent conflicts has required a continual process of negotiation and compromise at both the domestic and the international level. Governments have often had to adjust and put to positive use the constant tension between the forces of economic protection and trade liberalization.

For almost forty years, Canada has pursued a largely multilateral approach to its foreign economic policy; indeed we have been one of the strongest supporters of the multilateral system centred on the GATT and the International Monetary Fund. This approach was the most effective way to improve and secure access for our products and to instil order, stability and predictability into that process. Even on the import side, we have found that we must negotiate multilaterally to open our own market, in exchange for access to foreign markets. This action has proved a useful tool of industrial policy and has allowed for orderly adjustment of the economy through foreign competition.

To a great extent, Canadian trade policy has been, and will continue to be, developed as a trade-off between the business objective of securing improved access to foreign markets, the economic need to promote efficiency and competitiveness in the domestic economy, and the political need to maintain our sovereignty and freedom of action. The international trade and payments system largely determines the design and use of particular policy instruments. For Canadian producers and investors, there are several tests of this international system. Can our government successfully improve market access for those sectors where Canadian production is, or can be, competitive in world markets? Will it maintain current access available to Canadian producers? Will it protect producers from unfair or injurious foreign competition? Because private sector investment is necessary for growth and job creation, Canadian producers need to be confident that their access is secure, and that foreign governments will not move to frustrate the efforts to market Canadians goods abroad.

The multilateral system of rules is intended to facilitate decisions favouring adjustment and to penalize decisions favouring protection, but it needs political will to make it work. Between 1973 and 1979, the Tokyo Round of trade negotiations provided a framework for organizing political will. The negotiators sought to reduce trade barriers and to move the ongoing management of trade relations in the direction of freer trade. For the past six years, however, there has been no such framework.

A new round of GATT negotiations may be initiated, to concentrate on elaborating world trade law and removing remaining barriers to world trade, and to provide a basis for organizing political will to resist protection. The results of a future GATT negotiation are not certain, however, nor are they just around the corner. A new round of negotiations requires complex coordination and revolves largely around the interests of three or four players: the United States the European Community, the less-developed countries (LDCs) as a group, and perhaps, Japan. Canada can make an important contribution, but we cannot control either the agenda or the outcome. Even to influence the outcome requires adroit negotiators. The Community is reluctant to come to the table. The United States is eager, but as yet has no negotiating authority. The LDCs are willing, but insist on some problematic pre-conditions and do not agree on the agenda. Japan is willing, but largely because a new round would facilitate management of its trade relations with the United States and the European Community.

Canada's economic growth is critically dependent on secure access to foreign markets. Our most important market is the United States, which now takes up to three-quarters of our exports. More, better and more secure access to the U.S. market represents a basic requirement, while denial of that access is an ever-present threat. We are extremely vulnerable to any strengthening of U.S. protectionism. Early bilateral negotiations with the United States could provide opportunities for the two countries to negotiate reduction or elimination of tariff and other barriers to cross-border trade, at a pace and on a scale not likely to be achieved multilaterally in a further GATT round. Such negotiations could also be used to win agreement on rules designed to deal with special or unique problems affecting cross-border trade; they would provide a more secure shield against a U.S. policy of protection.

The pursuit of Canada-U.S. free trade is not at odds with efforts to strengthen and improve the existing multilateral framework. Rather, Commissioners see it as a complementary approach, involving concentration of our efforts and scarce resources on our most important market. We see multilateral negotiations proceeding in parallel. In our view, such a two-tiered approach is the best way to ensure that Canadian industry will win sufficient access to foreign markets to invest and grow with confidence. At the same time, it will allow us to open our market in an orderly fashion and thus ensure that trade policy does its part in encouraging the development of a more competitive and more productive economy.

Commissioners see negotiations with the United States as neither panacea nor disaster, but as a prudent course which will help to make us richer and, by making us richer, strengthen the fabric of our country and increase our self-confidence. While this course may initially make Canada more dependent on the U.S. market, it will offer our nation a more secure relationship and thus make us less vulnerable. Ultimately, it should strengthen and diversify our economy, achieving for us goals that we have long sought, but which have eluded us, largely because our domestic manufacturing sector has been too weak to attain them.

Negotiations leading to freer trade, whether pursued bilaterally or multilaterally, will be of little use if they are not supported by the right domestic policies. Our support for freer trade, therefore, depends in no small way on the recommendations Commissioners develop later in this Report. These recommendations should contribute to strengthening the competitiveness and productivity of Canada's domestic economy. Trade policy alone will not be enough.

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We believe that the approaches we recommend below will help to strengthen our country. They will allow Canadians to pursue the gradual transition from a staple economy to a fully-industrialized modern economy, living in harmony with, but distinct from, our friends and allies.

> **The Commission presents what might stand as the strongest argument for free trade - and the subtlest. It does not just argue that the benefits outweigh the costs. It goes further, and argues that what have always been counted as dangers will actually prove to be advantages.**
>
> **One claim against free trade, for example, is that it would tie the Canadian economy even more tightly as client and supplier to the dominant U.S. market. On the contrary, says Macdonald. Free trade would improve productivity, and better productivity would expand Canada's ability to trade with the rest of the world.**
>
> **Ottawa Citizen, September 7, 1985**

RECOMMENDATIONS

Having carefully considered the analyses presented above, Commissioners make the following general recommendations.

- Canadians have benefited from and contributed to the multilateral system of trade and payments developed primarily in the last 40 years, and we should continue to support that system as the main stay of our foreign economic policy. Canada is sufficiently strong and independent, however, to pursue bilateral initiatives, including better economic relations with the United States, within the framework of multilateral relations.

- Canadian import policy in general should be based on a recognition of its costs to consumers and the costs of delaying adjustment. Canada should minimize any new protection, reduce protection gradually as part of bilateral or multilateral negotiations, and accelerate adjustment processes.

- Export promotion should be pursued aggressively and with greater reliance on private sector mechanisms, but the degree of subsidization this may involve should be within internationally accepted rules and practices.

INTERNATIONAL TRADE

International trade is the life-blood of the Canadian economy. It is a major contributor to Canadian growth, jobs and real incomes. In view of the changing nature and patterns of international trade, Canadians are now confronted with several options in formulating trade policy. This Commission has identified three major approaches, each of which has several variations. Canada might:

- Maintain its present policy. It might keep to the level and type of protection currently in place, but make selective efforts both to improve access abroad and to protect Canadian industry on a limited case-by-case basis.

- Participate actively in a new round of multilateral trade negotiations under the auspices of the GATT, in order to improve and secure our country's access to foreign markets, to open up our own market, and to strengthen the legal framework for international trade.

- In addition to taking the initiative for the elimination of trade barriers at the multilateral level, open negotiations with the Government of the United States to reach an agreement on a substantial reduction of barriers, tariff and non-tariff, between Canada and the United States.

This Commission rejects any generalized move toward greater protection or toward import substitution as a general policy to insulate Canadian producers from the international economy. This approach, while perhaps the most comfortable in the short term, would lead, in the longer term, to major inefficiencies in the national economy, a loss of jobs and lower incomes, and would contribute to an erosion of the multilateral system. In our view, a policy of maintaining the status quo would carry the serious risk of taking Canada backwards to a more protectionist position.

Commissioners recommend that multilateral trade negotiations under the GATT remain a central theme of Canadian trade policy; thus Canada should move quickly to define its objectives for the forthcoming round. The GATT has served Canada well, and our nation's participation in further strengthening this international system of co-operation is a general insurance policy for the future. Broadly stated, Canada's objectives should include.

- A more ordered world trading environment: that is, sufficiently stable, predictable and transparent international trade relations to instill a degree of business confidence that will lead to job-creating investment

- More secure access to our major markets, particularly the U.S. market

- Improved opportunity for the further processing of our natural resources before export, by reducing foreign barriers to manufactured goods

- Improved access and trading conditions for agricultural and fishery products

- An improved framework of international rules which will encourage orderly adjustment in the Canadian economy.

Commissioners recommend that the Government of Canada, at the same time it undertakes an initiative at the multilateral level to eliminate trade barriers, open negotiations with the Government of the United States to reach agreement on a substantial reduction of barriers, tariff and non-tariff, between Canada and the United States. Such an agreement would have to stand within the terms of Article XXIV of the GATT, and it would provide for a reduction of barriers between the two countries, but would leave each country with freedom of action to maintain separate trading policies with other economic partners. We do not recommend a more intensive arrangement such as a common market or an economic union, where even closer integration would take place between these two economies.

- Commissioners recommend that Canada negotiate a legal arrangement with the United States which incorporates strong safeguards to limit spill-over from the arrangement and thus to protect substantive policies, such as those pertaining to culture and defence, which are functionally unrelated to trade in goods and services. Indeed, a policy that creates no linkage should be explicitly confirmed in order to avoid surprises if the Government of Canada, as we recommend, were to pursue a more aggressive policy of support for indigenous cultural expression as a concomitant of a bilateral trade initiative.

• Commissioners recommend that this legal arrangement attempt to regulate three general types of barriers that currently restrict trade between the two countries. We recommend that

- Tariffs be phased down to zero over a period of perhaps ten years. Effective rules of origin must be developed.
- An approach should be developed to use measures of contingent protection as follows:
  - For measures governing "fair" trade (such as safeguard action) and "unfair" trading practices (such as dumping and countervailing-duty proceedings), enforcement would be shifted from national administrative tribunals to a new Canada-U.S. intergovernmental body established under the arrangement; this body would be known as the "Canada-U.S. Trade Commission"(CUSTC).
  - Detailed codes of national conduct would be required to govern resort to other non-tariff measures such as discriminatory federal and state government/procurement practices, product standards and federal customs, classification rules and administrative procedures. Again, these matters should be subject to review of the CUSTC.

• The Commission holds that a free-trade arrangement should incorporate explicit provisions which reflect the proportionately greater costs of adjustment that Canadians will face. The Canadian economy needs more time for adjustment than does the U.S. economy. We therefore recommend a two-track approach to phasing in the tariff cuts to allow U.S. rates of duty generally to be reduced either at a faster rate or earlier than Canadian tariffs. The Canadian government should quickly develop strategies for adjustment which are compatible with the framework of adjustment assistance proposed in Part V of this Report, that is, the new Transitional Adjustment Assistance Program. The emphasis of government programs should be on assisting workers to adjust to new employment opportunities. In addition, a reoriented industrial policy, as set out in part III, will encourage the flexibility and growth orientation required by a freer-trade environment.

• This Commission recommends that the Government of Canada urge the Government of the United States to implement the free-trade arrangement by amending U.S. federal and, if necessary, state legislation to conform to the arrangement, and that they do so under a "fast track" procedure which would require Congress to pass implementing legislation within 90 days of the President's formal declaration that he intends to sign an international agreement binding the United States. We also recommend, however, that a formal treaty eventually be struck once both governments have had sufficient experience with the arrangement.

- This Commission recommends that negotiations in Canada proceed on the basis of a broadly based, federal-provincial consensus, and that provinces be prepared to give legislative assent to the provisions of the arrangement, in keeping with the high degree of consultation that will be required to achieve federal-provincial consensus. We also recommend that in the longer term, Canadian governments establish a federal-provincial constitutional procedure: sections of the treaty that impose obligations on provinces would come into effect across Canada when two-thirds of provincial legislatures, representing at least half of Canada's population, passed resolutions in support of the treaty.

- This Commission recommends the formation of a three-tiered Canada-U.S. intergovernmental institution to provide basic executive and administrative decisions; technical staff services; adjudication of complaints and appeals under the agreement. We further recommend the following mechanisms:
  - A committee of national officials at the ministerial level to be responsible for the enforcement of the agreement's obligations
  - A supporting body of officials known as the "Canada-U.S. Trade Commission"(CUSTC) to manage non-tariff barriers, but subject to appellate review by the Ministerial Committee
  - A standing arbitral panel with binding powers as a board of last resort, to resolve disputes arising from conflicting interpretations of the agreement. Such a panel would consist of two Canadians, two Americans and one neutral member to be chosen by the members of the panel.

- International trade and industrial policy are inextricably linked. In Canada, there is the added dimension of cultural and social implications. To undertake successful negotiations on freer trade with the United States will require an extraordinary management effort by the Government of Canada. Commissioners, while making no specific recommendation on how best to prepare the way for the negotiations, wish to express concern that the current federal departmental structure does not appear to provide the degree of integration required to carry out a major negotiation of this kind. It may be that an Office of the Special Trade Negotiator should be established, and that the incumbent should report directly to the Prime Minister.

REPORT ON MARKET ACCESS CONSULTATIONS*

This report summarizes the findings of detailed consultations undertaken between May 15 and September 5, 1985, following Mr. Kelleher's announcement of May 3rd, in which he established this phase of the consultative process to "provide one-stop shopping for business, labour, and other interested parties. In this way, all those seeking to convey their views on either multilateral or Canada-U.S. trade issues can do so through one central point in the Government."

In addition to the press release which was distributed very widely to interests in Canada known to be interested in these issues, specific invitations to participate were sent to major industry trade associations (139 in all) covering individual goods and services sectors, to the five leading labour organizations, and to about 50 representative companies, both large and small. Some 91 groups, organizations and individual companies responded to this invitation.

The consultations provided extensive coverage of a number of leading goods sectors; agriculture, fisheries and food processing; the lumber and pulp and paper industries; the mining, non-ferrous metals and steel sectors; the foundry sector, the plastics industry, the chemicals sector, machinery and equipment, including telecommunications, computer-related and other high technology sectors, transportation equipment, furniture, textiles, and the cosmetic, toiletry and fragrance sector. Representatives of other goods industries which participated include tires, business forms, toys, window and door manufacturers, shipbuilding and ship-repair firms, automotive after market parts, appliances, and the recreational boat industry.

It is worth noting that, in the absence of a clearly articulated position by the government, a number of groups came to the consultations with only general concepts of what a comprehensive trade agreement might cover. The concept of phasing in of trade agreement provisions over a significant period of time, the likelihood that such issues as contingency protection measures, and non-tariff barriers could be included in the negotiation of a trade agreement, and the possibility that the government might be prepared to consider adjustment assistance measures in the context of a broad ranging agreement were not always understood. During the discussions, when these questions were raised, a number of those who were opposed to a Canadian initiative appeared to be somewhat less concerned about the adverse impact on their particular industries.

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*The consultations were pursued on the basis that the views expressed would be held in confidence by the government and not associated with any group, organization or company. This report, therefore, summarizes the views expressed in aggregate terms.

Of those consulted, 52 groups were clearly in favour of the negotiation of a comprehensive trade agreement with the United States, 27 were opposed, and 12 were in an intermediate position (the latter included some which had not yet adopted a firm position, others which saw some benefits on individual issues, but not a comprehensive agreement, others which represented groups in which some members were in favour, others were opposed). There was no obvious correlation between position adopted and the size and/or location or ownership of those consulted.

The following sections of the report outline the main points made by those in favour and those opposed, report on the views about the investment potential of a comprehensive Canada-U.S. agreement, comment on some of the non-trade related policies which could have an effect on the potential of a new Canada-U.S. trade arrangement, note the views expressed about the role of exchange rates, and review the comments made about Canadian participation in a multilateral trade negotiation.

THOSE IN FAVOUR

The points of view expressed by those in favour included the following:

a) For those with existing large stakes and favourable terms of access to the U.S. market, including subsidiaries of U.S. corporations which already have, or are in the process of specializing and rationalizing on a North American basis, the principal concern is to avoid the application of more adverse terms of access to the U.S. through the application of U.S. contingency protection measures (e.g., anti-dumping, countervailing, or emergency safeguards), through Congressional actions or otherwise. These respondents are concerned about what they see as sharply increasing protectionist influences in the U.S. and would like to see Canada take steps to secure our access to the U.S. market.

b) As well, this group includes those who see the opportunity to increase substantially their sales to the U.S. market, and who would like to see improved as well as secure access to that market.

c) In addition to tariffs and contingency protection measures, those in favour of a comprehensive Canada-U.S. agreement would also welcome an extensive reduction or elimination of non-tariff obstacles to trade. The non-tariff barrier of most general concern relates to government procurement practices in the U.S. at the federal and state levels. Generally, a four-way reduction or elimination of federal and state procurement practices in the U.S. and the comparable federal and provincial barriers in

Canada is seen as the most desirable outcome. Indeed, some of those consulted viewed existing provincial barriers to trade with Canada as one of the most serious obstacles in their efforts to become internationally competitive.

A wide variety of other non-tariff barriers were noted by this group. A significant number are related to regulatory, inspection and standards questions, where the objective should be to achieve the maximum degree of consistency between Canadian and U.S. practices.

d) A few respondents noted the current tendency in the United States to move towards restrictions in the transfer of technology to Canadian firms, particularly in the defence-related industries, and would like to see this problem addressed in a Canada-U.S. agreement.

e) In terms of elimination of tariffs on both sides, there are three general points of view expressed by these groups. The first recommends the elimination of duties immediately at the conclusion of the negotiation; the second proposes a phase-in period of two to five years; and the third suggest a longer transition ranging from eight to ten years. Most recognize that the U.S. negotiating position will probably require an equal transition, product by product, on both sides of the border, but a few propose that the U.S. should eliminate its tariffs on the products of interest to them at a faster pace than the corresponding Canadian tariff disappears. There were also some who recommend that Canada and the U.S. identify some small grouping of products for which tariffs on both sides could be eliminated in advance of the conclusion of an overall agreement.

f) Those in favour are characterized by confidence in their competitive ability, by comparable unit labour costs, by world class technology, and in some cases by easy access to raw materials. Their concern about the Canadian scene is not about these elements, but about the need for macro economic policies in Canada which will underpin the competitive nature of the Canadian economy overall.

g) For many, bilateral trade liberalization with the U.S. was qualified as a forerunner of the required economies of scale without which Canadian industries cannot aggressively and successfully pursue export opportunities in offshore markets.

THOSE OPPOSED

In the consultations, those groups which are opposed to a comprehensive agreement with the United States, or which would wish to see themselves excluded from any such agreement expressed a number of general views, including the following:

a) A number point to the great disparity in industry and plant size between Canada and the United States, which puts Canadian operations at a substantial competitive disadvantage:

b) Productivity and unit labour costs are not competitive with U.S. counterparts, particularly those established in the U.S. South;

c) Those in this group which represent subsidiaries of U.S. parent companies indicate that their operations are typically small mirror images of the U.S. plants, and that relative costs are such that substantial investment would have to be made to bring Canadian plants up to standards competitive with those in the United States. These Canadian operations are typically aimed at satisfying the Canadian domestic market, and suffer from the resulting short runs of a large number of products. They have done little or nothing to move in the direction of specialization and rationalization with their parent companies.

d) In looking at the need for incentives to bring their plants up to competitive standards, they underline the difficulty of accessing such capital against the lower costs of capital in the United States, including state and municipal incentives, and the fact that increased marginal capacity increases in U.S. plants would be more effective to supply Canada in a free trade environment than substantial new Canadian capacity;

e) Those which represent smaller Canadian-owned businesses in this group tend to emphasize the relative under-capitalization of their current businesses, typically oriented towards the Canadian market only, and often have a current situation where U.S. tariffs are significantly lower than the corresponding Canadian tariff, a circumstance with which they are comfortable.

f) They tend to be skeptical that a comprehensive agreement can be successfully negotiated with adequate provisions to make Canadians confident that its elements will not be compromised in future.

g) If an agreement is negotiated and their products are not excepted, this group would want the longest possible transition period for the phasing in of Canadian tariff reductions, a differentially shorter period for U.S. tariff elimination, and safeguard measures to prevent surges of imports, particularly in the phase-in period. On this latter point, provisions to counter predatory pricing by U. S. companies which attempt to move into the Canadian market massively and quickly would be important to those consulted.

INVESTMENT

A variety of views were expressed about the impact on investment in Canada of a comprehensive Canada-U.S. agreement.

a) Typical of those in favour of such an agreement is the view that the current uncertain state of access to the U.S. market is a powerful factor inducing Canadian firms requiring a larger market than the domestic Canadian market to locate any additional capital investment in the United States rather than in Canada. Correspondingly, a tight Canada-U.S. agreement would reduce the influence of this factor, and provide an impetus to long overdue investments in some resource industries.

b) Some of those consulted believe that Canada will become a more attractive location for foreign investors should we have secure access to the United States. It was also suggested that if Canada were not to pursue a comprehensive agreement with the United States, this decision would be seen as one in which Canada is opting for a more "parochial" national economic objective, with long run adverse impact on investment flows.

c) Often those opposed to a Canada-U.S. agreement suggested that at worst there would be capital disinvestment in Canada and marginal increases in investment in the U.S. following an agreement. Among the points made, some of which are reported above, is the observation that investment incentives from States and municipalities in the U.S. are very attractive. Those in this category representing subsidiaries of U.S. firms believe that it would be important for their future in the event that they are included in an agreement to have available Canadian investment incentives to counter the weight of the preference for American investment and supply.

d) There is nervousness among a number of Canadian market oriented firms that the capital market in Canada is not adequately organized to provide the access to new investment resources which will be required to respond to the challenge of a wider market.

EXCHANGE RATE

Nearly all those consulted underlined the importance of future trends in exchange rates in any estimate of the effects of a closer trade relationship with the United States. Of the variety of views heard, the following three were most prominent:

1. If the Canadian dollar advanced in value in a gradual trend towards the 80¢ to 85¢ range, and this reflected a perception in the international money market that the Canadian economy was becoming relatively more competitive compared to the U.S., Canadian industry should be able to continue to compete effectively.

2. Some of those consulted believe that any significant increase in the Canadian dollar exchange rate would be damaging, particularly if the increase took place over a relatively short period and in response to capital movements occuring in advance of improvements in the basic competitiveness of the Canadian industry.

3. A number of respondents indicated that because some of their important inputs were priced in U.S. dollar terms a change in the Canada-U.S. exchange rate would have relatively little impact on their operations.

NON-TRADE RELATED GOVERNMENT POLICIES

All those consulted made the point that it was essential that Canadian policies should be aimed at making the macro economic climate in Canada the most internationally competitive possible. In addition, specific comments were made regarding the following:

1. Transportation

Many of those consulted emphasized the importance of transportation costs in their business. They recognize the advantage which U.S. companies now have in a de-regulated environment. All of those commenting on this issue expressed support for the de-regulation concepts outlined in the government's recent discussion paper on transport policy.

2. Competition

Three points emerged under this heading:

a) It is important in judging the competitive situation in Canada to regard the Canadian market as part of the larger world market, and in the context of a Canada-U.S. agreement, as part of a North American market and not to consider competition solely within the Canadian market itself. A comprehensive agreement with the United States will probably lead to increased pressure for mergers, etc., as small and medium-sized Canadian firms position themselves to compete effectively. Competition policy should promote this kind of activity.

b) The possibility of rationalizing product lines among Canadian firms in the same industry should be encouraged to promote the more rapid attainment of internationally competitive economies of scale.

c) Some of those consulted expressed interest in modifications to competition policy or anti-dumping to deal with potential predatory pricing by large U.S. corporations.

3. Taxation Policy

While the need to ensure overall competitiveness with the U.S. on total corporate tax burdens was underlined generally, some made further specific points:

a) The U.S. export tax incentive (FISC) would give U.S. exporters greater incentive to exploit a Canada-U.S. trade agreement than was available to Canadian exporters.

b) Investment incentives should be designed to encourage those (particularly the traditional style Canadian subsidiaries) who fear new investment in a freer Canada-U.S. trade environment taking place in the United States.

MULTILATERAL TRADE NEGOTIATIONS

Not surprisingly, the predominant focus of the consultations was on a possible Canada-U.S. initiative. Few, therefore, brought forward specific MTN interests to be discussed at this time but most indicated they would come back subsequently. There was broad support expressed for Canada's participation in the upcoming Multilateral Trade Negotiations (MTN), but some skepticism regarding the timing for the new Round. Many saw pursuit of the MTN as quite consistent with a bilateral initiative with the U.S. and contributing further to achieving market access enhancement objectives. A number of those consulted, whose trade interests are primarily in overseas markets, see an MTN as essential to addressing their interests in enhanced export access.

For those strongly favouring a Canada-U.S. initiative and anxious to pursue exports from this expanded base, the MTN was also seen as a means of opening up additional third markets. The EC, Pacific Rim and Latin America were identified in particular.

For resource-based industries interested in securing existing advantageous access to the U.S. market under a comprehensive agreement, tariffs, tariff escalation and a number of non-tariff barriers in overseas markets were identified as impediments to Canadian exports which they would like to see addressed in the context of the MTN. This group tended also to express the view that any bilateral initiative be consistent with the GATT and not adversely affect trade relations with third countries. A number of those consulted also saw the MTN as a means of improving Canada's competitive position in countries which currently extend preferential access to other competing suppliers, such as EFTA members and developing countries, particularly in resource related products.

For those concerned about the impact of eliminating Canadian tariffs under a Canada/U.S. initiative, the MTN was seen as providing scope for more limited cuts in Canadian tariffs and, possible, more palatable phase-in conditions for sensitive industries. But, those adamantly opposed to any Canada/U.S. initiative tended to express the same concern about MTN cuts in their existing tariff and regulatory protection.

The MTN was also seen by some of those who support the initiation of bilateral negotiation with the US as another mechanism for attempting to achieve Canadian trade objectives vis-à-vis the U.S. if the price under a comprehensive arrangement ultimately proves too high.

> **In assessing Canada's relationship to the global economy, our central theme has been the need to recognize that our social and economic well-being is dependent on being competitive internationally. To regain our competitiveness, we must adopt long-term policies based on economic realities which recognize our relationship with the U.S.**
>
> **Business Council of British Columbia**

TEXT OF REPORT BY THE MINISTER FOR INTERNATIONAL TRADE TO THE PRIME MINISTER

My Dear Prime Minister,

The March 18 Quebec Declaration on Trade in Goods and Services charged United States Trade Representative Clayton Yeutter and me to chart all possible ways to reduce and eliminate existing barriers to bilateral trade and to report to you and the President of the United States within six months. We have met several times in the interim and our officials have worked closely together.

I have now concluded that the time has come to explore more directly with the United States Administration the scope and prospects for a new trade agreement. We should advise the Administration of our intentions as early as possible to enable the Administration to consult with Congress and the private sector. I would envisage exploratory negotiations beginning early in 1986. I would see the period between then and now as providing an opportunity to continue consultations with the provinces, private sector and labour. Should negotiations start in January, your next meeting with the President in the spring of 1986 would provide an opportunity for a more definitive report on the nature and prospects for an agreement.

I see the broad objectives of such negotiations from Canada's perspective to be:

- to save jobs in the short term and create jobs in the medium and long term.
- to create a stronger economy in all regions of Canada.
- to stimulate balanced growth and job creation throughout the nation.
- to allow all Canadians to share in the benefits of this national effort.
- to strengthen the economic basis for our cultural objectives.
- to secure and enhance our access to the U.S. market by enshrining a better set of rules whereby our trade is conducted.
- to develop a more predictable environment for trade and investment.

We are also pursuing these objectives in GATT. Indeed, our commitment to the multilateral economic system should remain the cornerstone of our international trade policy. We are fully committed to a new round of multilateral trade negotiations. I am convinced that a process of complementary bilateral and multilateral trade negotiations will strengthen our economy, our capacity to compete in global markets, and our bilateral economic relations with Europe, Japan and the developing world. It would contribute significantly to our government's program of economic renewal. I am convinced further that this initiative with our major trading partner and an equally vigorous approach to a new multilateral trade negotiation will reinforce our ability to act independently and credibly in foreign policy.

I reached these conclusions on the basis of extensive, government-wide studies and analysis over the past six months, as well as wide-ranging consultations and discussions with Canadians from coast to coast. A high degree of dissatisfaction with the status quo was evident across the country. In every one of the fifteen cities I heard a consistent message. I was told repeatedly that the current level of unemployment is unsatisfactory and directly related to uncertainty in our trade relations with our principal trading partner. Clearly, for these Canadians, the status quo is not viable.

In recent months, I have met with my provincial counterparts on several occasions to tell them what I was hearing and to discuss the results of ongoing research and analysis. We have been encouraged and guided in our work by the outcome of trade discussions among First Ministers at the Regina Conference on February 14 and 15, 1985. My officials have also met regularly and frequently with their provincial counterparts. As a result, I am satisfied that there is a strong provincial consensus in favour of bilateral negotiations with the United States to secure and enhance our access to that market. During our consultations, I assured my provincial counterparts that the federal government would work closely with the provinces to ensure that their interests would be taken into account in any negotiation.

I also heard from many Canadians who are eager to seize the new opportunities which a successful trade negotiation would open up in a larger North American economy. They are confident that they could adjust to new circumstances. They echoed the need for a new and expanded trading relationship with the United States.

Canadian producers are concerned about their access to the U.S. market. More than two million workers depend on this access. In addition to problems arising from a lack of predictability, I was also informed of a number of specific barriers which many thought could and should be reduced. These included:

- the manner in which Canadian companies' access to the U.S. market can be frustrated by the use of trade remedy laws.

- the ease with which imports from Canada are swept up in measures aimed at others.

- the continual threat of unilateral changes in the rules of the game.

- the lack of access to the U.S. procurement market due to Buy America provisions at the federal and state levels.

- the large number of U.S. tariffs which continue to limit access to that market.

- the inadequacy of current mechanisms to resolve disputes.

These concerns were echoed in the report of the Special Joint Parliamentary Committee on Canada's International Relations which conducted public hearings in July and August. The Committee agreed that the status quo was not viable and urged the government to discuss the prospects for an agreement with the Americans. The Royal Commission on the Economic Union and Development Prospects for Canada also conducted extensive public hearings and engaged in detailed research and analysis of this issue. It also recommends that we proceed as quickly as possible to a process of bilateral trade negotiations with our principal trading partner.

A trade agreement will save Canadian jobs now threatened by protectionist measures in the short term and create better jobs for the future. Our goal should be to conclude arrangements which serve the interests of all Canadians and stimulate growth in all regions. We will need, however, to be sensitive to the concerns of those who consider themselves adversely affected. I believe their concerns can best be met through appropriate transitional measures.

During the consultations, many within our cultural communities expressed concern about protecting our sovereignty and culture. Our cultural identity, of course, is not for negotiation. Canada has reached a plateau of maturity which helps to define the opportunity before us. Our economic strength and cultural integrity have evolved to the point where we can enter negotiations with confidence. The very act of opening our minds to negotiations will be an expression of faith by Canadians in themselves, in their industries and in their institutions.

There are also Canadians who expressed concern about the extent and scope of any negotiations with the United States. They would be more comfortable if their particular economic interests would not be affected. I assured them this government will only pursue a negotiation which increases the well-being of all Canadians. An agreement which does not meet this test would not be of interest to Canada.

Some Canadians worry that the removal of tariff barriers will remove the incentive of U.S. multinational companies to continue to operate in Canada. Many businessmen have assured me that these companies are faced with exactly the opposite concern. They worry about current threats to their access to the U.S. market. With assured and improved access to a large market, they are likely to stay and expand.

The considerable research and analysis pursued over the past three years by the Royal Commission, research institutions, the universities and the federal and provincial governments have ensured we are adequately prepared for a trade negotiation. This work will contribute significantly to ensuring an early and fruitful start to negotiations.

Mr. Yeutter has indicated that the U.S. Administration would favour negotiations which would improve the access of U.S. investors and exporters to the Canadian market. He and I agree that our respective concerns and objectives are amenable to a mutually beneficial negotiating process.

Complementary bilateral and multilateral negotiations would respond to the commitment in the Quebec Declaration "to establish a climate of greater predictability and confidence for Canadians and Americans alike to plan, invest, grow and compete more effectively with one another and in the global market." I am confident that such negotiations can be pursued to Canada's benefit and in a manner consistent with our obligations under GATT. Indeed, I believe a successful negotiation with the United States will increase the prospect of meeting our other trade objectives in a multilateral trade negotiation.

I would also like to report on progress being made on the eight items identified in Quebec as specific impediments to trade. As you know, we have achieved an enhanced market approach in our energy trade. A good beginning has been made in improving the air transport agreement and facilitating travel for business and commercial purposes. Work is also proceeding on these matters as well as on ways to standardize, reduce or simplify regulatory impediments. Further work on government procurement, tariff barriers, barriers to trade in high-technology goods and services, and intellectual property rights should be included in the negotiations mentioned above.

These are the conclusions I have reached following nine months of consultation, discussion, analysis and informal talks with the Americans. As you know, I have kept you and our Cabinet colleagues regularly informed of my findings and tentative conclusions. Our discussions have reflected the growing awareness in the country that we have reached the point of decision. In my view, we should now proceed and send a signal of our readiness to the Americans. In doing so, we should be attentive to the concerns in various quarters of Canada and establish a consultative and negotiating structure capable of responding to these concerns.

James F. Kelleher
Minister for International Trade

"We're going to unify the country the way we've never done in the past".

John Bulloch, President of the Canadian Federation of Independent Business

"There's not an outerwear factory in the U.S. that I'm afraid of. Technologically, we have one of the best outerwear plants in the world."

M.L. Brownstone, Gemini Fashions, Winnipeg

TEXT OF REPORT BY UNITED STATES TRADE REPRESENTATIVE CLAYTON YEUTTER TO THE PRESIDENT ON BILATERAL TRADE WITH CANADA

The "Declaration by the Prime Minister of Canada and the President of the United States of America regarding trade in Goods and Services" issued at the Quebec Summit on March 18 charged the Minister for International Trade and me to establish immediately a bilateral mechanism to chart all possible ways to reduce and eliminate existing barriers to trade and to report to you and the Prime Minister of Canada within six months. Since I have assumed my duties as United States Trade Representative, I have met with the Canadian Trade Minister, James Kelleher, on several occasions to discuss ways to improve our bilateral trading relationship. In addition, our respective staffs have worked closely over the past six months to provide Minister Kelleher and me with specific advice. There are several ways in which we could reduce and eliminate barriers to our bilateral trade in goods and services. The most promising would be the exploration of a comprehensive bilateral trade negotiation.

We are committed to pursue negotiations aimed at a further liberalization of trade, be they on a bilateral, plurilateral, or multilateral basis. Over the past decade, Canadian and American Governments have been at the forefront of efforts to achieve a greater degree of global trade liberalization under the multilateral trading system based on the General Agreement on Tariffs and Trade (GATT). Both Canada and the United States are actively pursuing a strengthening of the multilateral system through a new round of multilateral negotiations under the auspices of the GATT.

Earlier this year, the Canadian Government initiated a review of options for securing and enhancing trade with the United States. Canada's interest in bilateral trade liberalization with the U.S. is understandable. Canada's exports constitute nearly one third of its GNP, and exports to the United States account for over 75 percent of its total exports. Exploiting additional economies of scale by expanding trade and obtaining greater security for its trade with the United States are, therefore, priority Canadian objectives.

From preliminary, informal discussions which my staff and I have held with representatives of the private sector and Members of Congress, I believe that a number of U.S. industries have an interest in expanding their access to a prosperous and proximate Canadian market. Canada takes nearly one-fifth of our total exports, and there exist significant barriers to U.S. exports of goods and services in a number of sectors. In particular, these include:

- high Canadian tariffs across a wide spectrum of products which act as major impediments to U.S. exports;
- nontariff barriers at both the federal and provincial level which effectively preclude many U.S. exports from entering the Canadian market;
- obstacles to U.S. investment; and
- federal and provincial regulations which impede U.S. exports of services.

In addition, a great many U.S. industries and Members of Congress have expressed concern over a number of governmental assistance programs, both federal and provincial, which allegedly result in subsidized competition. I have been urged to obtain in any bilateral discussions agreement on procedures to limit the use of subsidies.

My discussions with Trade Minister Kelleher indicate that the Canadian Government is prepared to seriously explore these issues. Minister Kelleher shares my belief that they could be best addressed in a bilateral negotiation which would complement your efforts to launch a new round of multilateral trade negotiations. Clearly, any bilateral negotiation would be pursued in a manner consistent with our GATT obligations.

If the Canadian Government announces its desire to explore bilateral negotiations with us, I recommend that we begin consultations with the Committee on Ways and Means of the U.S. House of Representatives and the Finance Committee of the U.S. Senate on their views regarding possible negotiations with Canada. I further recommend that other domestic procedures be initiated in order to ensure that all interested parties have an opportunity to advise on any potential negotiations. These procedures include seeking the advice of the U.S. International Trade Commission, holding public hearings by the Executive Branch, and extensive consultations with our private sector advisory committees.

I would also like to report on progress being made in achieving results on the eight items identified in the trade declaration of March 18, 1985 as specific impediments to trade. I believe that, should bilateral trade negotiations commence, further work on government procurement, tariff barriers, barriers to trade in high technology goods and services, and intellectual property rights be subsumed in these negotiations. Our discussions aimed at achieving an enhanced market approach in our bilateral energy trade have been successful. A good beginning has also been made in improving the bilateral air transport agreement and facilitating travel for business and commercial purposes. Work is proceeding on these matters as well as on means to standardize, reduce and simplify regulatory requirements which would facilitate trade in goods and services. Minister Kelleher and I will report to the Prime Minister and you on further progress in six months time.

Minister Kelleher will be reporting along similar lines to Prime Minister Mulroney.

> The best method of negotiating Canada's trade policy problems with the United States is not necessarily by means of a multilateral bargaining forum. Of course, it can be argued that the only way Canada can negotiate lower U.S. tariffs is by combining its own leverage with the bargaining power of other countries adhering to the GATT. This is sometimes true: the Tokyo Round agreement on the civil aircraft sector is an important example. But one should not automatically assume this to be true simply because the multilateral technique of past tariff negotiations was so productive. In the case of negotiations on other types of barriers or devices, it is less likely to be true, and it may be even less true for the remaining tariff issues.
>
> Rodney de C. Grey, An Agenda for Canadian-U.S. Relations

TEXT OF STATEMENT BY PRIME MINISTER BRIAN MULRONEY ON CANADA-USA TRADE NEGOTIATIONS

Mr. Speaker, I rise to inform the House and the country that I have spoken today to the President of the United States to express Canada's interests in pursuing a new trade agreement between our two countries.

We hope that this action will lead to negotiations for a new trade agreement between the United States and Canada. I have asked the President to explore with Congress their interest in pursuing these negotiations. Both sides recognize that the issues are complex. Both sides are determined to see the process move as expeditiously as possible.

The President and I will be meeting in the spring of 1986 to review progress and the prospects for a new agreement.

Honourable Members will recall that at Quebec City six months ago, President Reagan and I made a declaration on trade in goods and services. We pledged to explore all possible ways to reduce and eliminate existing barriers in our bilateral trade. We instructed the Minister for International Trade and the President's Trade Representative to report on how trade could be enhanced between our two countries. Today I will table the Minister's report to me on this vitally important subject.

Throughout our history, trade has been critical to Canada's livelihood. Now, almost one third of what we produce is exported. Few countries in the world are so dependent on trade. Yet, our share of world trade has been declining. This trend ultimately threatens the jobs of many Canadians and the living standards of the nation as a whole.

We must confront this threat. We must reverse this trend. To do so, we need a better, a fairer, and a more predictable trade relationship with the United States. At stake are more than two million jobs which depend directly on Canadian access to the U.S. market.

Five decades ago the world was in the midst of the Great Depression. Restrictive trade policies made things worse. Canada and the United States were the first to respond to the strong protectionist pressures of the time. They began the process of tearing down these obstacles to growth. Canada and the United States concluded a bilateral trade agreement in 1935. More countries joined them in 1938. And the principles underlying the Canadian-American bilateral agreement formed the foundation of the post-war multilateral trading system.

Ottawa **Statement by the Prime Minister** **September 26, 1985**

> **Mr. Mulroney's statement (in the House of Commons) . . . is realistic: it opens the door to a major agreement with the United States while respecting the rights of Canadians to define the contents of the agreement as negotiations proceed.**
>
> **La Presse, September 27, 1985**

For half a century Canada has pursued a policy of trade liberalization. Today more than ever, our prosperity and that of our partners depend on an expanding world trade and a growing world economy. In all the international forums where Canada is present, we are working to remove impediments to trade, aid, investment and development on a global basis.

In particular we are playing a leading role in promoting and preparing for a new round of multilateral trade negotiations in the GATT. We are consulting the less developed countries on issues of common concern; and we emphatically support their participation in the negotiations.

Economics, geography, common sense and the national interest dictate that we try to secure and expand our trade with our closest and largest trading partner. To do so is fully consistent with our commitment to freer trade on a multilateral basis. Of course any new agreement between Canada and the United States would have to meet the test of our over-riding obligations under the GATT.

Five decades ago, national governments turned inward to shield their peoples from economic distress. Ultimately, protectionism proved suicidal. It brought on the Great Depression with all its attendant misery.

No responsible person anywhere today advocates protectionism as a national economic strategy. Yet, sector by sector, region by region, country by country, Canada included, there persists the impulse to protectionism, whenever the going gets tough. Protectionist measures are always advocated as exceptional cases.

But the barriers grow more numerous, more ingenious and more insidious all the time. Sometimes these measures are aimed directly at Canadian products or services; often they are aimed at others, but catch us in the process. The motive may be laudable. The effect may be incremental. But in any overall reckoning, protectionist measures are always self-defeating. This impulse to protectionism is defensive and negative -- yet entirely understandable in human terms. This is what we are up against.

The answer to this problem lies in sound agreement, legally binding, between trading partners, to secure and remove barriers to their mutual trade. That is our approach to world trade. And it is obvious that we must find special and direct means of securing and enhancing the annual $155 billion of two-way trade with the United States.

The government will be pursuing clear goals in our talks with the United States. We are two sovereign democracies, sharing the same continent, reaching out with maturity and strength to seek out ways of enhancing mutually beneficial trade goals.

The need to secure our access to the U.S. market was the dominant theme of representations made in all parts of the country to the Minister for International Trade during his extensive consultations last spring and summer. The same message was heard by the Senate-House of Commons Committee which reported in late August. Honourable Members will have taken note of the conclusions of the Macdonald Commission together with its impressive analysis and documentation.

Canadians will also be aware of the very strong representations on trade which have been made by their provincial Premiers over the past several months. I have taken care, and shall continue to take special care, to consult with my fellow First Ministers, as the process unfolds. To that end, I have placed this major issue on the agenda at the meeting of First Ministers in November. The government will also arrange, if possible, a debate in this House on the subject of trade at a time agreeable to Honourable Members.

We must all be aware that international negotiations are complex and extremely challenging. Success is not a sure thing but the results of success are well worth the enormous effort and good faith required for the negotiations. Moreover, we have already agreed to establish a special mechanism with the provinces, to assure their continuing involvement throughout the process. To support Canada's negotiating effort, the Minister for International Trade is creating a new consultative arrangement with businessmen, labour and other groups.

I emphasize that we are beginning a process of purely commercial negotiations with the United States, the results of which would provide sufficient time for all Canadians to plan ahead to take advantage of new opportunities from enhanced access.

We seek to negotiate the broadest possible package of mutually beneficial reductions in tariff and non-tariff barriers between our two countries. We are not negotiating a customs union, a common market or any other economic arrangement which would affect our own independence or our relations with the rest of the world.

I accept the words of prudence coming to us from some quarters on this subject. We understand the natural concerns of various sectors and regions that their interests be recognized both in the negotiations and in any agreement.
There is general consensus, however, that we must seek to secure and improve our trade with the United States. To shrink from this challenge and opportunity would be an act of timidity unworthy of Canada. It would be contrary to the national interest.

Our political sovereignty, our system of social programs, our commitment to fight regional disparities, our unique cultural identity, our special linguistic character - these are of the essence of Canada. They are not at issue in these negotiations. They will be stronger in a Canada made more confident and prosperous from a secure and dynamic trade relationship with our biggest customer and with all the world.

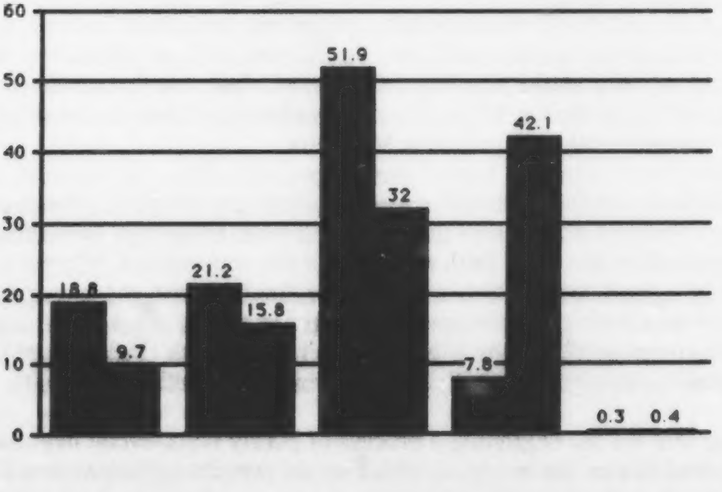


CHART 8
% Commodity Composition of Canadian Exports, 1960/1984

Mulroney-Reagan Exchange of Letters

Text of letter from Prime Minister Mulroney to President Reagan

OTTAWA
October 1, 1985

Dear Mr. President,

Last March you and I issued an important Declaration on Trade in Goods and Services. We agreed "to give the highest priority to finding mutually acceptable means to reduce and eliminate existing barriers to trade in order to secure and facilitate trade and investment flows."

I would, now, like to propose that our two governments pursue a new trade agreement involving the broadest possible package of mutually beneficial reductions in barriers to trade in goods and services. Such an agreement should secure and enhance access to each other's markets by reducing and eliminating tariff and non-tariff barriers and result in a better and more predictable set of rules whereby our trade is conducted.

I understand that the Administration is consulting the Congress on this proposition. I hope that this process will move swiftly. We look forward to hearing from you on the results of these consultations in order that we can move to negotiations. It should then be possible for you and me to review progress at our next meeting in the Spring of 1986.

The negotiation of a new trade agreement will, of course, be extremely arduous. The challenge to succeed, however, and the fruits of success, are well worth the enormous effort and good faith required for this initiative.

Sincerely,

Brian Mulroney

Text of Letter from President Reagan to Prime Minister Mulroney

WASHINGTON
October 2, 1985

Dear Mr. Prime Minister:

It was good to speak to you last Thursday and to receive your letter proposing to explore more directly the scope and prospects for a bilateral trade agreement. I welcome this proposal. As you know, I am committed to the pursuit of free and fair trade and I believe our objective should be to achieve the broadest possible package of mutually beneficial trade barrier reductions. If history has taught us one thing, it is that the freer flow of world trade, the stronger the tides for human progress and peace among nations.

My Administration is beginning consultations with the Congress and the private sector to get their views regarding negotiations with Canada. As I mentioned to you, I want to see this process moved as promptly as possible. I, too, look forward to reviewing progress at our meeting next year.

Nancy joins me in wishing you, Mila and your children, especially your new son, all the best.

Sincerely,

Ronald Reagan

CANADIAN STATEMENT TO THE SPECIAL SESSION OF GATT CONTRACTING PARTIES

Mr. Chairman,

Canada welcomed and strongly supported the request of the United States to convene a special session of the contracting parties to discuss the subject matter and the modalities of a new round of multilateral trade negotiations. Canada is fully engaged in promoting and preparing for the new trade negotiations along the lines described in our submission to the GATT in July. We hope that all contracting parties that rely on international markets for their economic well-being will also see it in their own best interest to participate constructively in this cooperative undertaking.

We now have an opportunity to get down to work seriously and to co-operate for common purposes and objectives. Indeed, this meeting constitutes an important milestone because it marks the start of the preparatory process towards the new round of multilateral trade negotiations. We are setting in motion a process that will ultimately determine whether confidence in the multilateral trading system can be restored, a sine qua non of present and future economic growth on which the well-being and stability of all our countries crucially depend. A successful MTN will strengthen the hands of our respective governments to preserve and enhance the access to markets so painfully negotiated in previous MTNs. It will find solutions to old and new trade problems and by so doing modernize the framework for the conduct of our mutual trade relations now and in the future.

It cannot be overemphasized that a liberal trading system, based on agreed and transparent rules, is essential to world economic growth. Of course, it is not the only element. Sound national macroeconomic policies, strengthened international economic policy co-ordination, further progress in adjusting to current imbalances and appropriate exchange rate relationships all have a role to play. In this context, I believe that recent co-operative efforts to achieve more sustainable exchange rate relationships are to be welcomed. It has become amply evident in recent years that without appropriate exchange rates the trading system is subject to increasing strain and pressure . However it is well to emphasize that there is an important reverse relationship too. Protectionist measures, particularly those undertaken by major trading countries, will not only slow growth but will inevitably lead to misaligned exchange rates and will seriously exacerbate the global debt problem. The lesson is clear. Current trade problems need to be addressed in concert with ongoing efforts to strengthen the international trade and payments system.

The status quo is not viable. As we have been coming out of the difficult economic recession, it has become quite clear that the new growth opportunities will require an improved climate and greater confidence by our respective producers to plan, to invest and to compete with one another in the global market. There is a worry in the Canadian business, farming and fishing communities and in our labour groups, that the stability and predictability of access to markets is seriously threatened by protectionist pressures. Developing a more predictable environment for trade and investment and enlarging market access is thus a fundamental task for us.

It seems to the Canadian Delegation that the key questions are:

- Will the new MTN be a timely and credible response to the serious challenges confronting all of us? We believe it can be but this is why the MTN preparatory process must be convincingly seen as being underway now.

- Will the MTN agenda be broadly based so as to reflect the legitimate interests of all countries? Clearly this has to be the case at the outset if the negotiations are to be meaningful.

- Will the MTN be a genuinely open negotiating process without preconditions and without prejudice as to the nature of potential trade-offs and linkages between issues and sectors? We strongly believe that the questions of linkages essentially concern individual national negotiating strategies and properly belong to the later stages of the negotiating process.

- Will the MTN seek to reform and update the existing trade rules or will it favour a static, narrow and legalistic view of the trading framework embodied in GATT? It would be naïve and reckless to believe that the credibility and effectiveness of the multilateral trading system could be restored if we do not seek to address new issues as they impact on trade. Let's remember that two of the most important achievements of the Tokyo Round, the Government Procurement Agreement and the Technical Barriers Code, were areas not traditionally covered by GATT. The elaboration of these instruments benefited importantly from extensive and productive contributions from a number of developing country delegations.

- Will the preparations of the new MTN proceed in the same spirit of co-operation as for previous rounds held under the auspices of the GATT? It is useful to bear in mind that just as no contracting party can be forced to accept agreements resulting from multilateral trade negotiations, other contracting parties cannot be denied the possibility to negotiate mutually beneficial trade advantages. Canada has long believed that the national interests of all countries are best served by a full participation in these negotiations. The alternative to the opportunity to influence the shaping of trade ground rules is to accept that these rules will effectively be established unilaterally, and perhaps arbitrarily, by the strongest trading partners in dealing with problems as they arise.

Mr. Chairman, these are some of the key questions which, in the view of the Canadian delegation, need be answered positively and in a forward looking manner if we are to discharge properly our collective responsibilities.

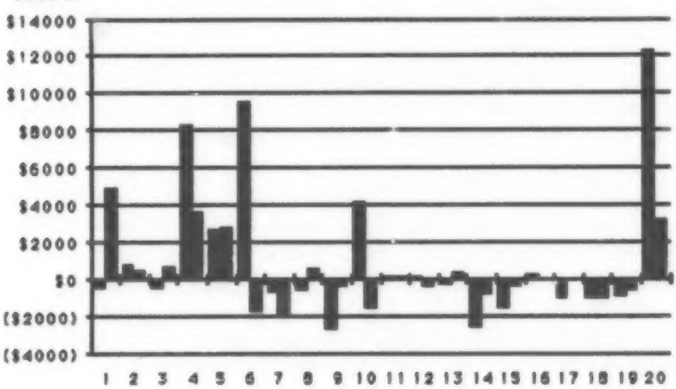
Finally, Canada believes that, in addition to defining further the content of the MTN agenda in which high priority must be accorded the 1982 Work Programme, this Session must also begin to explore the nature of the preparatory mechanism which should be put in place in the near future. We believe a preparatory committee must soon be established to develop clear recommendations on how negotiations on all agenda items should be conducted. Such a committee, in our view, should indentify methods and procedures for negotiations with the full and active support of existing GATT committees and groups.

In conclusion, Mr. Chairman, we cannot afford to mark time. If we do not meet the challenges before us, we will surely also fail to create the growth opportunities which trade expansion would bring and which all our economies and societies need so much.

> Finally, what is required is not so much a change in Canadian policies as a change in Canadian attitudes. Canada, after all, is -- through GATT -- already committed to the abolition, virtually, of tariffs on trade with the United States, and to the maintenance of the free flow of information and entertainment, which together ensure the continuing integration of the two societies. But instead of regarding this prospect with foreboding, as a defeat for Canadian nationalism and a threat to sovereignty and identity, Canadians should be encouraged to see it as an opportunity to knock down barriers, thereby enlarging their opportunities to compete and to demonstrate the virtues of their society.
>
> Anthony Westell, "Economic Integration with the USA," International Perspectives, November/December, 1984.

CHART 9

Canadian Trade Balances by Sector: 1985
United States and Rest of World



LEGEND

1. Agriculture and food
2. Fish and fish products
3. Miscellaneous crude & fabricated materials
4. Forestry products
5. Metals & minerals
6. Energy
7. Textiles, clothing & footwear
8. Chemicals & petrochemicals
9. Machinery & equipment
10. Automotive products.
11. Urban transportation
12. Ocean & marine industries
13. Aircraft
14. Electronics
15. Electrical machinery & equipment
16. Furniture
17. Scientific & medical equipment
18. Miscellaneous consumer products
19. Special transactions
20. All sectors

TRADE NEGOTIATIONS AND CULTURAL INDUSTRIES

BY THE RIGHT HONOURABLE JOE CLARK
SECRETARY OF STATE FOR EXTERNAL AFFAIRS

In September, 1985 the Prime Minister announced that Canada would enter discussions with the United States to explore the scope and prospects for a new bilateral trade agreement. I have since met with Secretary of State George Shultz who indicated to me that the United States Government would be ready to begin these discussions early in 1986. The President has now notified the Congress of his intent to enter into negotiations with Canada. Between now and next spring, we will intensify the process of consulting with Canadians and further develop our strategy and negotiating mandates.

There have been suggestions that commercial trade negotiations with the United States could erode our cultural identity if Canadian cultural industries are not excluded from such negotiations. Such statements suggest there may be some misunderstanding as to what a trade negotiation is about, and of even greater importance, what a trade negotiation is not about. As this distinction is fundamental to bilateral trade negotiations with the United States as well as the forthcoming multilateral trade negotiations, I believe it warrants explanation.

What are the international trading rules and how can they be improved through trade negotiations? The General Agreement on Tariffs and Trade (GATT) covers cultural industries like any other industry. Through GATT negotiations, Canada and many other countries have agreed not to impose customs duties on many cultural products and to reduce duties on inputs to products used by the cultural industries like cameras, directors' chairs, recording tape, sound equipment, and fine paper for books and magazines. In the last round of multilateral trade negotiations (the Tokyo Round), the United States lifted a restriction which prevented Canadian book printers from selling freely in the U.S. market. The next round of multilateral trade negotiations will be a further chance to reduce the customs duties and other trade barriers which still exist.

What we, as a Government, will be seeking through negotiations has been clear for sometime: we want a better, more predictable and more secure trading relationship with our major trading partners so that Canadian enterprises can plan, invest and grow with confidence, the kind of confidence that leads to more and better jobs. Of particular interest is the United States market which now takes three-quarters of our total exports. What will be involved? These will be commercial negotiations between two distinct and sovereign countries. But we all know that modern nations are more than economic. The challenge will be to strengthen both our economy and our sovereignty.

We and the Americans will be working towards a package of mutually beneficial and mutually acceptable reductions in tariff and non-tariff barriers in order to increase trade and thereby save jobs and create new jobs in the future. In order to get a good deal, both sides will have to be prepared to listen to the other. We want the United States to consider our concerns about the protectionist effect of their trade remedy legislation, our desire to gain greater access to their government procurement market, and the need for a more effective and predictable way to settle our differences. They will want us to listen to their concerns about our high tariffs, about our industrial support programs, about our investment rules and about international rules regarding trade in services. By listening to each other -- by placing these concerns on the table -- neither side is committed to accepting what the other side is proposing. But only by frankly discussing each other's objectives and concerns will we know whether a good deal is possible. We are prepared to do that. As the Prime Minister indicated in his September 26 announcement, if a deal which is good for all regions and all Canadians is not negotiable, there will be no deal.

It is virtually impossible to reach a good deal by placing the negotiators in a straitjacket of exemptions before they even sit down. Exemptions invite further exemptions and can eventually ensure that a good deal is no longer achievable. Being prepared to sit down does not mean you will give up those things that are important, that are part of our national heritage, that are integral parts of things Canadian. Rather, being prepared to talk about them is to ensure that you can continue to do things the Canadian way, can continue to protect our heritage, and are freed from the tyranny of ad hoc solutions.

Culture is an elusive concept. It is the embodiment of a nation's nature and spirit. It is the heritage that is handed down to succeeding generations. It is how we define ourselves to ourselves, and to others. This implies domestic encouragement and international exposure. Cultural industries are the commercial enterprises that transmit cultural expression, at home and abroad.

As we enter trade negotiations, some in Canada are extremely concerned with the effect these negotiations might have on Canadian cultural industries and therefore on our ability to express and develop our national sovereignty. I respect their concern. Two questions are at issue. One is the vitality and support of Canadian culture. The second is the negotiation of trade rules that might affect cultural industries. We need to distinguish between these questions.

Our government's intention to promote culture in Canada through direct financial support is simply not at issue in a trade negotiation. The issue of whether or not specific Canadian cultural industries require special measures to assist them is a a domestic issue that falls outside trade negotiations. We do not expect the extensive framework of American government support for similar institutions in the U.S. to be considered in trade negotiations either.

No country is more open than Canada to foreign cultural products. Anyone who doubts that should look at our book stores, our theatres, our cinemas, our magazine racks, our broadcasting system, our galleries and museums. Equally, no country in the world is more committed than Canada to making the rules of international commerce more transparent and fair.

But not all sectors are of equal weight. Canada, as do other countries, reserves the right to make distinctions between sectors based on certain explicit criteria. The United States casts the net of "national security" over more areas than does Canada; Canadians cast the importance of cultural identity more widely than do Americans. Canada's commitment to maintaining a vibrant, independent cultural identity should not stop us from seeking better trade rules for cultural industries. From the federal government's point of view, better rules are both possible and desirable.

We are prepared to discuss with the United States whatever concerns it may have. We expect a similar openness on their side. No doubt, as the negotiations progress, the U.S. side will state that it cannot meet certain Canadian demands; no doubt we will do the same. This is how negotiations work.

But we can make certain understandings explicit. We are prepared to discuss with the United States ways we can strengthen cultural industries through trade. Under no circumstances are we prepared to agree to any measure which weaken those Canadian industries or undermine their capacity to serve our cultural needs.

Canadian culture is strong and vibrant and it will grow and flourish. But I am acutely conscious that Canadian culture and the Canadian economy must grow together. This government believes we can strengthen our cultural identity while at the same time building on our economic relationship with the United States. That is the modern reality in Canada.

There is a relationship between this Government's desire to assist, promote and encourage the growth and vibrancy of Canadian culture both at home and abroad, and our willingness to sit down with our trading partners to work out a fairer, more predictable environment for all industries, including cultural industries. We will not be dissuaded, however, from exploring with our biggest and best customer, the benefits and opportunities trade negotiations might have to offer. At a minimum, we need to consider together, through discussions and consultations, what we need to preserve and what we stand to gain. We may have differences in view, but we must all be prepared to exchange views and to explore together what a trade negotiation means.

Exempting cultural industries from the negotiation at the outset will mean that the general benefits that will result from the negotiation in terms of more secure access, better rules and more predictable channels for resolving differences of view will not be available to that industry. I can see little benefit to Canada from such an approach.

On the other hand, enhancement of trade with the United States could strengthen our economic base and provide us with increased means to finance excellence in education, the arts, science and technology, social programs, international development and national defence. That would strengthen our sovereignty and reinforce our sense of pride as a people.

Increased prosperity lets us pursue Canadian social and cultural policies appropriate to our own conceptions, values and needs. That is the essence of sovereignty -- being able to do what we want to do. What limits us today is not our will but our economy. Icebreakers cost money. So do dance troupes and social programs, and the other instruments of sovereignty.

The question of Canadian identity is not new to me. For eight long months, four years ago, I fought and changed a constitutional measure, precisely because I believed it offended the nature of my country. In two public incarnations, I have had the honour to help the Canadian people express our nature in response to foreign crises, once in Ethiopia, once on the Indo-Chinese seas, with acts of generosity and sacrifice. Like my Prime Minister, and many of our colleagues, I came into active politics in response to Mr. Diefenbaker's vision and had the honour, earlier this year, to announce sovereign decisions to strengthen that northern integrity which he proclaimed.

I know something about this country -- its strength, its contradictions, its sense of vulnerability. My own view is that, in recent years, we have become much stronger, as a national community, much more sure of our ability to compete.

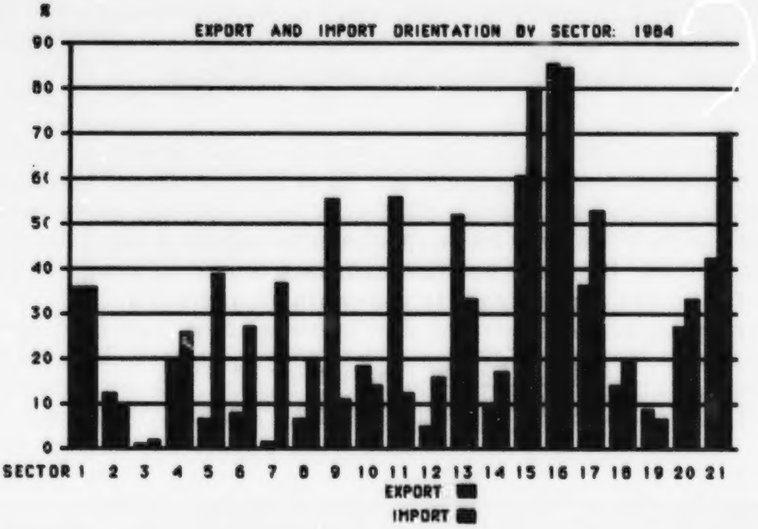
The decision to open negotiations with the United States will not weaken our sovereignty or our identity. It is an assertion of sovereignty in an increasingly interdependent world. It demonstrates our confidence that we can be as productive, innovative, ingenious and efficient as our American partners.

As the Prime Minister stated in the House of Commons on September 26: "International negotiations are complex and extremely challenging. Success is not a sure thing but the results of success are well worth the enormous effort and good faith required for the negotiations". This challenge exists for all industries and all Canadians. We are confident we can meet that challenge.

> There seems little point at this stage in listing what is not negotiable; the more positive approach would be to learn first what our partners to the south want from a new trade agreement.
>
> Calgary Herald, September 27, 1985

> A trade negotiation is a search for mutual advantage, and the job of our guys is to get the best deal they can for us. Anyone who thinks the Americans won't or shouldn't try to do the best they can for themselves is living in a dream. What the trade negotiation will not be about is free lunch for every Canadian.
>
> Christopher Young, Ottawa Citizen, November 7, 1985

CHART 10



LEGEND:

1. All sectors
2. Food and beverages
3. Tobacco products
4. Rubber and plastics
5. Leather
6. Textiles
7. Knitting mills
8. Clothing
9. Wood industries
10. Furniture and fixtures
11. Pulp and paper
12. Printing and publishing
13. Primary metal
14. Metal fabricating
15. Machinery
16. Transportation equipment
17. Electrical products
18. Nonmetalic minerals
19. Petroleum and coal
20. Chemicals
21. Miscellaneous manufactures

PART III:

BACKGROUND INFORMATION

> Apart from these considerations, Canadians should understand why this move is so vital. If Canada is to compete not only in the U.S. but in the world, its industries must be built to the efficiency-scale of large markets. That requires massive investment which will not be forthcoming without some guarantee that U.S. competitors will not mire Canadian industry in Washington's elaborate system of trade litigation. The Macdonald Commission really discovered that much of Canadian industry is not afraid to compete with America, it is afraid to invest if it won't be allowed to compete.
>
> Halifax Chronicle-Herald, September 28,1985

GLOSSARY OF TRADE TERMS

Term	Definition
Adjustment	The ongoing process by which the economy declines or renews and adjusts to changing circumstances. Among the factors which influence the scope and pace of adjustment are changes in technology and productivity, trade liberalization, consumer taste, resource exhaustion, and the changing composition of the labour force.
Anti-dumping Duties	Additional duties imposed by the importing country in instances where imports are priced at less that the "normal" price charged in the exporter's domestic market and are causing material injury to domestic industry in the importing country.
Autopact	A sectoral trade agreement entered into by the United States and Canada in 1965 in order to encourage the rationalization and growth of the North American auto industry. It provides for duty-free movement between the two countries of new automobiles and original equipment parts.
Common Market	See Customs Union.
Competition Policy	Set of policy measures whose objective is to protect the effective operation of the economy based on the premise that generally a market system will give better results in terms of economic and industrial performance than any alternative systems of industrial organization. Canada's competition policy is founded in the *Combines Investigation Act*.
Contingency Protection	Collective term referring to Anti-dumping and Countervailing Duties and Safeguards.
Countervailing Duties	Additional duties imposed by the importing country to offset government subsidies in the exporting country,

	when the subsidized imports cause material injury to domestic industry in the importing country.
Customs Duties	See Tariff.
Customs Union	A group of nations which have eliminated trade barriers among themselves and imposed a common tariff on all goods imported from all other countries. A customs union is often referred to as a common market.
Defence Production Sharing Arrangements	A set of administrative arrangements between the United States and Canada dating back to the 1941 Hyde Park arrangement providing for free trade in defence materiel and encouraging shared production of such materiel.
Dispute Settlement Mechanism	Those institutional provisions in a trade agreement which provide the means by which differences of view between the parties can be settled.
Duties	See Tariff.
Escape Clause Measures	See Safeguards.
Emergency Restrictions	See Safeguards.
Fair Trade	See Unfair Trade.
Framework Agreement	A trade agreement limited to a broad statement of objectives but including institutional arrangements to facilitate the attainment of these objectives.
Free Trade	An economic concept used for analytical purposes to denote trade unfettered by government-imposed trade restrictions; also used as a general term to denote the end result of a process of trade liberalization. Freer trade is the comparative term used to denote circumstances between current practice and the achievement of free trade.

Free Trade Area	A cooperative arrangement among two or more nations which agree to remove substantially all tariff and non-tariff barriers to trade with each other, while each maintains its differing schedule of tariffs applying to all other nations.
Functional Trade Agreement	A trade agreement limited to a particular type of measure used to restrict or manage trade, such as government procurement, emergency safeguards or countervailing duties.
GATT	The General Agreement on Tariffs and Trade (GATT) is a multilateral treaty, subscribed to by 91 countries or contracting parties which together account for more than four-fifths of world trade. GATT delineates rules for international trade. Its primary objective is to liberalize world trade and place it on a secure basis, thereby contributing to global economic growth and development.
Government Procurement	The term refers to purchases of goods and services by official government agencies. As a non-tariff barrier to trade, it refers to discriminatory purchases from domestic suppliers, even when imported goods are more competitive.
Import Quota	See Quantitative Restriction.
Injury	The term used in international commerce to describe the effect on domestic producers of a decline in output, lost sales, decline in market share, reduced profits and return on investment, reduced capacity utilization, etc., as a result of import competition. A distinction is often made between serious injury (required for emergency safeguard measures) and material injury (required for anti-dumping and countervailing duties).
Intellectual Property	A collective term used to refer to new ideas, inventions, designs, writings, films, etc. protected by copyright, patents, trademarks, etc.
Most-Favoured-Nation Treatment (MFN)	A commitment that a country will extend to another country the lowest tariff rates it applies to any third

	country. This is the first principle of the GATT. Exceptions to this basic rule are allowed in the formation of regional trading arrangements, provided certain strict criteria are met.
Multilateral Trade Negotiations (MTN)	Series of negotiations culminating in simultaneous agreements among participating countries to reduce tariffs and non-tariff barriers to trade. Seven rounds of multilateral negotiations have been held under the auspices of the GATT since 1947.
National Treatment	This expression refers to the extension to imported goods of a treatment no less favourable than that accorded to domestic products with respect to internal taxes, laws, regulations and requirements. GATT members are obliged to accord to one another "national treatment" with respect to internal measures that can affect trade.
Non-Tariff Barriers Measures	Government measures or policies other than tariffs or which restrict or distort international trade. Examples include import quotas, discriminatory government procurement practices, measures to protect intellectual property.
Phasing	See Transitional Measures
Quantitative Restriction	An explicit limit, usually by volume, on the amount of a specified commodity that may be imported into a country.
Round	The term used to describe the periodic trade liberalization conferences sponsored by the GATT. Seven rounds have been held since 1947, the latest of which was the Tokyo Round (1973-1979).
Rules of Origin	The term for the set of measures used to differentiate between goods originating in one country from those in another for the purpose of the application of trade measures such as tariffs. For example, goods made up of components originating in various countries but which when assembled add 50% to their overall value may be considered to be goods originating in one

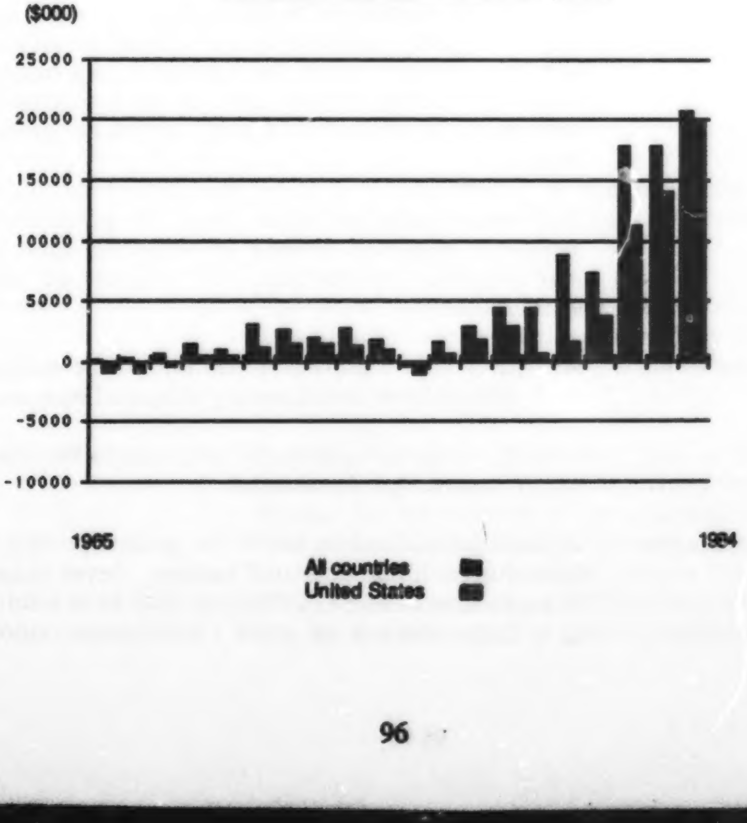
country, whereas the addition of 25% in value would not qualify. Such rules are very important for countries which are members of a free-trade area.

Safeguards	The term safeguards refers to emergency actions in the form of additional duties or import quotas applied to fairly traded imports which nevertheless cause or threaten serious injury to domestic producers.
Sectoral Trade Agreement	A trade agreement limited in its application to a particular group of related products comprising a sector. The Autopact is an example of a bilateral sectoral agreement and the GATT Aircraft Agreement is an example of a multilateral sectoral agreement.
Services	Economic activities the result of which is the provision of services rather than goods. This includes such diverse activities as transportation, communications, insurance, banking, advertising, consulting, distribution, engineering, medicine, education, etc. It is the fastest growing area of economic activity in Canada. Two-thirds of working Canadians are now employed in the services sector. Trade in services takes place when a service is exported from a supplier nation to another nation, such as an international airflight, or the extension of credit, or the design of a bridge.
Subsidy	A bounty, grant or other form of government assistance bestowed directly or indirectly upon the manufacture, production, or export of any merchandise.
Surcharge or surtax	A tariff or tax on imports in addition to the existing tariff, often used as an emergency safeguard measure.
Tariff	A tariff is a tax on imports; the tariff rate is the rate at which imported goods are taxed.
Trade Liberalization	A general term used to denote the gradual process of removing tariff and non-tariff barriers. Seven rounds of negotiations under GATT since 1947 have resulted in a large measure of trade liberalization among

	industrialized countries.
Transitional Measures	Those measures in place for a limited period of time during which a new trade agreement is gradually implemented. The Tokyo Round tariff cuts, for example, are being phased in over a period of eight years. Other transitional measures could include, for example, the right to take certain temporary safeguard measures or apply adjustment assistance measures.
Unfair Trade	An American term used to describe trade in dumped, subsidized or counterfeit goods; the application of the term has steadily widened as U.S. trade remedy laws have defined new practices which are considered to harm the export and import interests of U.S. companies.

CHART 11

MERCHANDISE TRADE BALANCE: 1965-1984
ALL COUNTRIES AND THE UNITED STATE



LIST OF BACKGROUND STUDIES

Sectoral Analysis

An interdepartmental team developed detailed sectoral profiles of the goods producing sectors of the economy. The main headings in each profile are as follows:

- Scope of Sector and its Place in the Economy (GDP, employment, exports, imports, etc.)
- Structural Characteristics (number of firms, location, ownership, strengths and weaknesses, etc.)
- Market Access Impediments and Vulnerabilities (key tariffs, non-tariff measures, etc.)

Profiles were prepared for some 25 goods-producing sectors, organized as follows:

1. Agricultural and Food Products

• Livestock and meat	Prepared by the Department ofAgriculture, with the Department of Regional Industrial Expansion (DRIE) for some sectors
• Dairy products	
• Grains and oilseed products	
• Fruits and vegetables	
• Forage seeds and nursery stock	
• Food processing	
• Alcoholic beverages	

2. Energy and Resource-based Products

• Fish and fish products	Fisheries and Oceans
• Energy products	Energy, Mines and Resources (EMR)
• Non-ferrous metals	EMR & DRIE
• Non-metallic minerals	"
• Forest products	Agriculture & DRIE
• Petrochemicals	DRIE & EMR

3. Fabricating and Manufacturing

• Rubber, chemicals and plastics • Iron and steel • Metal fabricating • Machinery • Transportation equipment • Electrical equipment • Printing and publishing • Footwear and leather • Textiles and knitting • Clothing • Furniture and fixtures • Miscellaneous products	Department of Regional Industrial Expansion (DRIE)

This material will provide the background to the preparation of more detailed negotiating mandates. They will be considered by the provinces and the trade advisory system. Some of the provinces are preparing similar material from a regional point of view.

Policy Papers

In order to provide a more informed basis for consideration of what are the issues and what is negotiable, a number of policy papers were prepared on key issues. In addition, a number of studies were contracted out to recognized outside experts. Policy papers have been prepared on the following subjects:

Safeguards Measures
Anti-dumping and Countervailing Measures
United States Trade Remedy Laws
Trade in Services
Government Procurement
Investment Issues
Interprovincial Barriers to Trade
Institutional Issues (Dispute Settlement)
Intellectual Property (copyright, trademarks, patents)
Agricultural Trade Issues
Policy Harmonization Issues (agriculture, trade remedy laws, subsidy practices, tax policy, cultural policy, commercial policy)
Competition Policy
Consumer Interests

Background Information

Research and Development
High Technology
Adjustment
The Autopact
The EC Experience

> **But the country can be certain of one thing -- if there are no discussions, there will be no opportunities for Canada to increase its trade in the huge U.S. market. And for a nation that lives on sales to markets outside its own borders, it would be folly to refuse to even discuss new trade deals. To be too fearful of possible consequences would be to invite greater economic isolation.**
>
> **Saskatoon Star Phoenix, October 1,1985**

CANADA-UNITED STATES TRADE NEGOTIATIONS: QUESTIONS AND ANSWERS

Why should we negotiate with the United States?

- to secure our access to our principal market in the face of growing protectionism. Without an adequate shield, thousands of jobs are at risk.
- to provide Canadian industry with the basis (unimpeded access to market of 250 million people) to restructure to meet global competition. A more competitive Canadian economy means more and better jobs.
- to clarify and codify rules, definitions and disciplines giving producers and investors greater certainty and confidence to expand and specialize.
- to improve access to world-class technology, knowledge and processes to help Canada meet the challenge of world competition.

What are the benefits?

- a more productive and efficient economy able to compete globally as well as with the United States.
- a better and more secure relationship with our principal customer and supplier.
- a boost in our wealth.
- lower prices for consumers.
- an enhanced ability to influence decisions in Washington which affect our well-being, i.e., within a better framework of rules.

What would we seek?

• **security**	- curbs on the U.S. capacity to restrict Canadian imports (better rules of the road).
• **enhancement**	- relief from Buy America provisions - broad elimination of U.S. tariffs.
• **enshrinement**	- institutional provisions to commit Congress and the Administration, to settle disputes and to implement the agreement in an equitable and bi-national manner.

How would we pay?

- reciprocal curbs on our capacity to restrict U.S. imports.
- reciprocal elimination of tariffs over broad range of sectors (phased in over a period of years).
- reciprocal openings on government procurement.
- new rules on investment and services.

Is such a deal negotiable?

- preliminary discussions with U.S. Administration and Congressional spokesmen suggest all these issues are open to meaningful negotiations.
- negotiations could start with everything on table, but allow exemptions and

special categories to emerge through negotiation.

- need to preserve room for negotiation, i.e., avoid the strait-jacket of preconditions and special interests.

What are the potential problem areas?

- short-term adjustment for some sectors of the economy. This would require adequate phasing and transitional arrangements once the shape of a final package is determined.

What is the difference between Canada-United States Negotiations and the MTN?

- the best overall approach would be to pursue and achieve our objectives multilaterally. In today's circumstances, however, relying solely on a new round of multilateral trade negotiations means that we would have to change our priorities. Some issues can only be addressed bilaterally; others can be addressed more quickly on a bilateral basis.
- there are now many more players with a wider range of objectives than in the past leading to a lower common-denominator result multilaterally and at a slower pace.
- Active Canadian participation in a new round, however, is not at issue. We will seek many of the same objectives multilaterally for other markets that we are now seeking directly with the United States.
- bilateral negotiations will be fully compatible with our GATT obligations.

What is the price if we don't proceed?

- We must recognize the interdependence of the world economy. A status quo policy would blunt the basic international economic realities facing Canada.
- To be successful in international trade, we must make sure that our goods and services are competitive in both quality and price.
- We have to reinforce a favorable climate for the growth of emerging technologies and industries of the future, to save the jobs we have now and to create new and better quality jobs in the future.
- We need to encourage a business environment that provides more certainty

and predictability and hence a more confident basis for investment, expansion, modernization and specialization.

- Canadian companies require stable and expanded access to the U.S. market in order to make firm and viable business decisions that lead to investment and job creation in Canada. They need secure access to large markets in order to lower their costs of production and increase their competitiveness.
- The current ad hocery in bilateral trade relations leads to insecurity and lack of predictability . Such an environment discourages investment. In its place we need trade rules agreed to by both sides that are fair and balanced for both countries. We need orderly and managed change to a North American economy.
- Protectionism leads to retraction of the economy, and ultimately loss of employment, loss of competitiveness and higher prices for consumers. We need to halt protectionist pressures in both the U.S. and Canada. Just opening negotiations provides an improved basis for resisting protectionism.

How long would bilateral negotiations take?

- formal negotiations could begin in 1986.
- process would take minimum of 18 to 24 months.
- implementation/transitional arrangements could be phased in over 5-10 years.

> **You'll bring out the best if you know you've got to face the best in the world. We can move into the U.S., which is the biggest free market in the world, and we can compete in it, and we can win.**
>
> **Andrew McMahon, Executive Vice-president, Marketing and Technology, Northern Telecom Canada Ltd.**

> **The case is gaining force, and the Macdonald report adds some cogent arguments. It uses the recent history of western Europe to show that the fears of loss of independence or identity may be overstated and perhaps completely wrong. . . . Macdonald doesn't offer a trade treaty as a cure-all, but he says it's the best hope for improving our economic performance, and thus our success in serving other goals, both at home and abroad.**
>
> **Christopher Young,**
> **Ottawa Citizen, September 7, 1985**

FURTHER READING

Perhaps no subject has been as much studied and debated in Canada's history as Canada-United States trade and economic relations. Various aspects of the issue have generated a large and interesting literature. The following suggestions for further reading, therefore, can do no more than point the way.

The most recent and thorough examination of the issue of Canada-United States freer trade can be found in the *Final Report* of the Macdonald Commission and in its supporting research. In the report, the section on Canada-US freer trade is found on pp. 215-385 of Volume One. Of the supporting research, Vol. 11, *Canada-United States Free Trade*, ed. by J. Whalley; Vol. 13, *Trade, Industrial Policy and International Competition*, by R. Harris; Vol. 29, *The Politics of Canada's Economic Relationship with the United States*, ed. by D. Stairs and G. R. Winham and which contains a good historical overview of the issue by J. L. Granatstein, "The Issue That Will Not Go Away"; and Vol. 53, *Canadian Economic Development and the International Trading System*, by M. M. Hart, are all of direct interest.

A very readable and persuasive introduction to the issue of freer trade can be found in Richard G. Lipsey and Murray G. Smith, *Taking the Initiative: Canada's Trade Options in a Turbulent World*, published by the C. D. Howe Institute (Toronto, 1985). A somewhat shorter introduction can be found in Anthony Westell, "Economic Integration with the United States," *International*

Perspectives, November/December, 1984. *Toronto Star* columnist Richard Gwyn has just completed a very personal account in *The 49th Paradox* (Toronto, 1985).

The Standing Senate Committee on Foreign Affairs under the chairmanship of Senator van Roggen examined Canada-United States relations at great length between 1976 and 1982. Particularly pertinent is Volume III of its report, *Canada's Trade Relations with the United States* (Ottawa, 1982).

A handy overview of various perspectives on this issue can be found in a special supplement (VIII of October, 1982) of *Canadian Public Policy*, edited by J.M. Curtis and A.R. Moroz, *Canada-United States Trade and Policy Issues*. Particularly useful is an article by R. S. Saunders, "Continentalism and Economic Nationalism in the Manufacturing Sector: Seeking Middle Ground."

The best introduction to the GATT and Canada's place in the international economic system can be found in Frank Stone, *Canada, the GATT and the International Trade System* (Montreal, Institute for Research on Public Policy, 1984). For the more specialized reader, the proceedings of a symposium on trade policy held in 1983 by the Institute for International Economics, edited by William R. Cline, *Trade Policy in the 1980s* (Washington, 1983) is replete with insight into the general trade policy challenges of the 1980s.

Two studies by Rodney Grey have set the tone for much of current consideration of the problems of the U.S. system of contingency protection for exporters to the United States market: *Trade Policy in the 1980s: an Agenda for Canada-U.S. Trade Relations* (Montreal, C.D. Howe Institute, 1981) and *United States Trade Policy Legislation: A Canadian View* (Montreal, Institute for Research on Public Policy, 1982)

A good overview of the Canada-United States relationship can be found in a collection of essays prepared for discussion at a symposium at Arden House in Harriman, New York last November and edited by Charles F. Doran and John H. Sigler, *Canada and the United States: Enduring Friendship, Persistent Stress* (Englewood Cliffs, New Jersey, 1985).

Volume 10 of the *Canada-United States Law Journal* contains the proceedings of a symposium held earlier this year on *The Legal Aspects of Sectoral Integration between the United States and Canada.*

The Canadian-American Committee, jointly sponsored by the C.D. Howe Institute in Canada and the National Planning Association in the United States, has published many books and pamphlets advocating economic cooperation.

Background Information

Among recent publications of interest are David Leyton-Brown, *Weathering the Storm: Canadian-U.S. Relations, 1980-83* (Toronto and Washington, 1985); Peter Morici and Laura L. Megna, *Canada-United States Trade and Economic Interdependence* (1980); Peter Morici, Arthur J. R. Smith and Sperry Lea, *Canadian Industrial Policy* (1982); and Peter Morici, *The Global Competitive Struggle: Challenges to the United States and Canada* (1984).

The Institute for Research on Public Policy will make available on request a discussion paper originally prepared for the Department of External Affairs, *Economic Effects of Trade Liberalization with the USA: Evidence and Questions*, by A.R. Moroz and Gregory J. Meredith (Ottawa, 1985).

A good general introduction to Canadian trade policy is contained in *A Review of Canadian Trade Policy* (Ottawa, Department of External Affairs, 1983).

CHART 12

CURRENT ACCOUNT BALANCE: 1965-1984
THE UNITED STATES AND THE REST OF WORLD